SUBJECT INDEX

PAGE

Petition for Writ of Certiorari 1
Summary Statement of the Matter Involved 1
Statement of Facts 2
Jurisdiction 9
Questions Presented 10
Reasons Relied on for Allowance of Writ 14
Prayer 18

Brief in Support of Petition for Certiorari 19
Opinion of Court Below 19
Jurisdiction 19
Statement of the Case 20
Specification of Errors Intended to Be Urged 22
Summary of the Argument 24
Argument 26
I. The Circuit Court of Appeals had no Power in this Proceeding to Grant a Priority or to Subordinate Creditors on Equitable Considerations 26
II. A. Respondents had no Vested Right Entitling Them to Priority in Any Event 37
B. Applicability and Effect of the Chandler Act 46
III. The Court Erred in Failing to Decide the Procedural Questions 50
Conclusion 53

Appendix A (Chapter X, Article XII, Secs. 222-4, 228, 236, 238) 54
Appendix B (Section 77B, Secs. (c (8)), (g), (h), (k) 57
Appendix C Section 64 (a) 60
Appendix D Rule 75 (a), (h), (j), Rules of Civil Procedure 62
Appendix E (Rule 13, 1, 6, Revised Rules of the Tenth Circuit 63

INDEX OF CASES CITED

PAGE

A.

Adams v. Bowen, 46 Fed. (2d) 294 (1st Cir. 1931) 39
American Serv. Co. v. Henderson, 120 Fed. (2d) 525 (4th Cir. 1941) 38
Amick v. Columbia Cas. Co., 101 Fed. (2d) 984 (8th Cir. 1939) 27
Ansaldo San Giorgio v. Rheinstrom Bros., 294 U. S. 494, 79 L. Ed. 1016 ..... 16, 17

B.

Bird and Son Sales Corp. v. Tobin, 78 Fed. (2d) 371 (8th Cir. 1935), 100 A.L.R. 654 33
Bronx Brass Foundry, Inc., v. Irving Trust Co., 297 U. S. 230, 80 L. Ed. 657 51
Burton Coal Co. v. Franklin Coal Co., 67 Fed. (2d) 796 (8th Cir. 1933) 29

C.

Callaghan v. R.F.C., 297 U. S. 464, 80 L Ed. 805 39
Campbell v. Alleghany Corp., 75 Fed. (2d) 947 (4th Cir. 1935, cer. den. 56 S. Ct. 92) 39, 42, 44
Carpenter v. Wabash, 309 U. S. 23, 84 L. Ed. 558 ..... 15, 38, 50
Case v. L. A. Lbr. Prod. Co., 308 U. S. 106, 84 L. Ed. 110 44
Chelsea v. Dolan, 24 Fed. (2d) 522 (1st Cir. 1928, cer. den. 72 L. Ed. 1012) 38
Chi., Milw. & S. P. Ry. v. Coogan, 271 U. S. 472, 70 L. Ed. 1041 17
Cons. Rock Prod. Co. v. DuBois, dec. Mar. 3, 1941, 85 L. Adv. Op. No. 9, 603 14
Cont. Ill. Nat'l Bank & Tr. Co. v. Chi., R. I. & P. R. R. Co., 294 U. S. 648, 79 L. Ed. 1111 39
Crowder v. Allen-West Com. Co., 213 Fed. 177 (8th Cir. 1914) 34
Cumberland Glass Co. v. DeWitt, 237 U. S. 447, 68 L. Ed. 1042 40

D.

Dallas v. Ryan, 62 Fed. (2d) 959 (5th Cir. 1933) 29

PAGE

Davis v. Louisville Trst. Co., 181 Fed. 10 (6th Cir. 1910) 28
Duke Power Co. v. Greenwood Co., 299 U. S. 259, 81 L. Ed. 179 18

F.

Fisher v. Pauline O. & G. Co., 309 U. S. 294, 84 L. Ed. 764 15

G.

Ginsberg v. Lindel, 107 Fed. (2d) 721 (8th Cir. 1939).... 46

H.

Hancock Mut. Life Ins. Co. v. Bartels, 308 U. S. 180, 84 L. Ed. 176 15
Hi-Flier Mfg. Co. v. Haberman, 115 Fed. (2d) 918 (2nd Cir. 1940) 48

I.

Inland Dredging Corp., 61 Fed. (2d) 765 (2nd Cir. 1932, cert. den. 77 L. Ed. 985), 88 A.L.R. 254..... 39
In re Bowman Hdw. & Elec. Co., 67 Fed. (2d) 792 (7th Cir. 1933) 36
In re Calif. Pea Prod. Co., 37 F. S. 659 (Cal. 1941)..... 48
In re Carden, 118 Fed. (2) 677.....16, 30
In re Central Fund. Corp., 75 Fed. (2d) 256 (2nd Cir. 1935) 39
In re Centralia Ref. Co., 35 F. S. 599 (Ill. 1940)..... 48
In re Chi., R. I. & P. Co., 90 Fed. (2d) 312 (7th Cir. 1937, cert. den. 82 L. Ed. 554), 113 A.L.R. 487.....39, 46
In re Collins Hosiery Mills, 18 F. S. 90 (Pa. 1937).....30, 48
In re Columbia Ribbon Co., 117 Fed. (2d) 999 (3rd Cir. 1941) 15, 29, 31, 48
In re Corona Radio & Telev. Corp., 102 Fed. (2d) 959 7th Cir. 1939) 43
In re Deep Rock Oil Corp., 113 Fed. (2d) 266 (1940)....17, 42
In re Eastern Utilities Inv. Corp., 98 Fed. (2) 620 (3rd Cir. 1938) 41
In re Higgin Mfg. Corp., 19 F. S. 120 (Ky. 1937)..... 49
In re J. B. Pollak Co., 86 Fed. (2d) 99, (2nd Cir. 1936).... 40
In re Laubheim Bros., 22 Fed. (2d) 910 (2nd Cir. 1937).. 40

PAGE

In re Kenilworth Bldg. Corp. 105 Fed. (2d) 673 (7th Cir. 1939) 49
In re Mallow Hotel Corp., 29 F. S. 931 (Pa. 1939) 43
In re Manhatta Music Hall, 14 F. S. 48 (N. Y. 1936) 49
In re Old Algiers, Inc., 100 Fed. (2d) 374 (2nd Cir. 1938) 38, 49
In re Ostlind Mfg. Co., 19 F. S. 836 (Ore. 1937) 30, 48
In re Pacific Oil & Meal Co., 24 F. S. 767 (D. C. Cal.) 31
In re Paramount Publix Corp., 82 Fed. (2d) 230 (2nd Cir. 1936) 43
In re Prima, 88 Fed. (2d) 785 (7th Cir. 1937) 38, 45
In re Roger Williams Bldg. Corp., 99 Fed. (2d) 212 (7th Cir. 1938, cert. den. 59 S. Ct. 1032) 43
In re Rosenbaum Iron Corp., 112 Fed. (2d) 315 (7th Cir. 1940) 36, 38

K

Keppel v. Tiffin Sav. Bank, 197 U. S. 356, 49 L. Ed. 790 32
Kuehner v. Irving Tr. Co., 299 U. S. 445, 81 L. Ed. 340 ..... 38, 44, 46

L

Lawson v. U. S. Min. Co., 207 U. S. 1, 52 L. Ed. 65 17
Local Loan Co. v. Hunt, 292 U. S. 234, 78 L. Ed. 1230 31
Lott v. Salisbury, 237 Fed. 191 (4th Cir. 1916) 29

M

Mesker v. Ohio Riv. Sand Co., 285 Fed. 379 (6th Cir. 1910) 28
Meyer v. Kenmore Granville Hotel Co., 297 U. S. 160, 80 L. Ed. 557 ..... 16, 41
Miners Sav. Bank v. Joyce, 97 Fed. (2d) 973 (3rd Cir. 1938) 49
Mohonk Realty Corp. v. Wise, 111 Fed. (2d) 287 (2nd Cir. 1940) 43

N

Nassau Smelt. & Ref. Co. v. Brightwood Bronze F. Co., 265 U. S. 269, 68 L. Ed. 1013 40

PAGE

National Lock Co. v. Hogland, 101 Fed. (2d) 576 (7th Cir. 1938) 43

P

Palmer v. Conn. Ry. & L. Co., dec. Jan. 6, 1941, 85 L. Ed. Adv. Op. No. 5, 283 14
Palmer v. Mass., 308 U. S. 79, 84 L. Ed. 93..... 15
Palmer v. Webster & Atlas Nat. Bank, dec. Feb. 3, 1941, 85 L. Ed. Adv. Op. No. 7, 436..... 15
Panama Mail Ss. Co. v. Vargas, 281 U. S. 670, 74 L. Ed. 1105 17
Pepper v. Litton, 308 U. S. 295, 87 L. Ed. 281..... 9, 16, 31, 32, 33, 43

R

Reconstruction Fin. Corp. v. Prudence Sec. Adv. Group, dec. Jan. 6, 1941, 85 L. Ed. Adv. Op. No. 5, 300..... 18
Reynolds v. Imlay, 118 Fed. (2d) 53 (C.C.A. D. C., 1941) 52

S

Sampsell v. Imp. Paper & Co. Corp., dec. Apr. 28. 1941, 85 L. Ed. Adv. Op. No. 13, 797..... 14
Schuyler v. Littlefield, 232 U. S. 707, 58 L. Ed. 710..... 36, 38
Sec. & Exch. Com. v. U.S.R. & Impt. Co., 310 U. S. 434, 84 L. Ed. 1293..... 15, 16, 31
So. Bell Tel. & Tel. Co. v. Caldwell, 67 Fed. (2d) 802 8th Cir. 1933) 29
Swan v. Children's Home Soc., 67 Fed. (2d) 84 (4th Cir. 1933) 38

T

Taylor v. Standard Gas & Elec. Co., 306 U. S. 307, 83 L. Ed. 669 ..... 9, 16, 32, 33
Thompson v. Magnolia Pet. Co., 309 U. S. 478, 84 L. Ed. 876 ..... 15, 16
Thompson v. Siratt, 95 Fed. (2d) 214 (8th Cir. 1938)..... 39, 44, 45

PAGE

U

U. S. V. Golden, 34 Fed. (2d) 367 (10th Cir. 1929) 37
U. S. v. Heinszen, 206 U. S. 370, 51 L. Ed. 1098 43
U. S. v. Marxen, 307 U. S. 200, 83 L. Ed. 1222 38
U. S. Rubber Co. v. American Oak L. Co., 181 U. S. 434, 45 L. Ed. 938 16,32
Union Joint Stock Land Bank v. Byerly, 310 U. S. 1, 84 L. Ed. 1041 15

W

Weil v. Nary, 278 U. S. 160, 73 L. Ed. 243 51
Wells v. Lincoln, 214 Fed. 227 (9th Cir. 1914) 32
Wiggin Terminals v. Hassett, 35 F. S. 654 (Mass. 1941) .. 42
Woods v. City Nat. B. & T. Co., dec. Feb. 3, 1941, 85 L. Ed. Adv. Op. No. 7, 478 15
Wright v. City Nat'l Bank, 104 Fed. (2d) 285 (6th Cir. 1939) 42
Wright v. Union Cent. L. I. Co., dec. Dec. 9, 1940, 85 L. Ed. Adv. Op. No. 3, 166 14

TEXTS CITED

PAGE

American Law Reports, Vol. 100, p. 660 34
Remington on Bankruptcy, Vol. 6, 4th Ed.,
Section 2778, pp. 329, 330 29
Section 2875, pp. 477, 483 30
Section 2839, p. 417 29

STATUTES AND RULES CITED

CHAPTER X OF THE CHANDLER ACT (See Appendix A)

Article III, Section 115 (11 U.S.C.A. 515) 47
Article XI, Section 222 (11 U.S.C.A. 622) 3, 13
Article XI, Section 223 (11 U.S.C.A. 623) 3, 13
Article XI, Section 224 (11 U.S.C.A. 624) 13
Article XI, Section 228 (11 U.S.C.A. 628) 13
Article XII, Section 236 (11 U.S.C.A. 636) 4, 9, 12, 13, 15. 20, 22, 46, 48
Article XII, Section 238 (11 U.S.C.A. 638) 9, 11, 12, 13, 15, 20, 22, 26, 30, 48, 49
Article XVI, Section 276 (c) (11 U.S.C.A. 676 (c)) 47

SECTION 77 B (See Appendix B)

Section (a) (11 U.S.C.A. 207 (a)) 47
Section (c) (8) (11 U.S.C.A. 207 (3) (8)) 30, 47
Section (f) (11 U.S.C.A. 207 (f)) 12, 41
Section (g) (11 U.S.C.A. 207 (g)) 9, 12, 23, 40, 41
Section (h) (11 U.S.C.A. 207 (h)) 12, 41
Section (k) (11 U.S.C.A. 207 (k)) 9, 11, 22, 24, 30, 47

OTHER SECTIONS OF BANKRUPTCY ACT (See Appendix C)

Section 1 (11 U.S.C.A. 1) 27, 33
Section 2 (11 U.S.C.A. 11) 27, 33
Section 24 (11 U.S.C.A. 47) 27
Section 63 (11 U.S.C.A. 103) 27, 49
Section 64 (11 U.S.C.A. 104) 8, 11, 20, 24, 26, 30, 48, 49
Section 65 (a) (11 U.S.C.A. 105) 32

JUDICIAL CODE

Section 240 (11 U.S.C.A. 347) 10

PAGE

RULES OF CIVIL PROCEDURE FOR THE DISTRICT COURTS OF THE UNITED STATES (See Appendix D)

Rule 75 (h) 13, 14, 51, 52
Rule 75 (j) 8, 18, 19
Rule 83 51

REVISED RULES OF THE CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT (See Appendix E) 8, 13, 52

GENERAL ORDERS IN BANKRUPTCY—No. 37 51

RULES OF THE DISTRICT COURT, DISTRICT OF COLORADO,
Rule 13, Sec. 1 51

IN THE

Supreme Court of the United States

No. .....

EARLE F. WINGREN, Trustee in Bankruptcy of The Mutual Investment and Security Company, Bankrupt,
Petitioner and Appellee Below,

vs.

MINNIE C. HANSSEN, THYRA H. MANKIN BERGER, W. J. O'NEILL, J. F. McGRAW, CATHERINE J. HANNA, P. B. McATEE, MAY WALSHE, FRANCES E. JOHNSTON, E. F. MITCHELL, KATE A. MITCHELL, MARGARET SWINK, LAURA E. PARKER and ALBERT J. GOULD,
Respondents and Appellants Below.

PETITION FOR WRIT OF CERTIORARI

To the Honorable Supreme Court of the United States:

I.

SUMMARY STATEMENT OF THE MATTER INVOLVED

Petitioner seeks a review of a final judgment of the Circuit Court of Appeals for the Tenth Circuit wherein the court refused, in a bankruptcy proceeding which followed the failure of a confirmed but only partially consummated plan of reorganization initiated under Section 77B but adjudicated under Chapter X, Article XII, of the Chandler Act, to apply the provisions of either Act relating to classi-

fication of claims. The controversy appealed was between the trustee (petitioner) and respondents involving certain claims which had been filed by respondents as secured claims based on the order confirming the plan of reorganization, and which had been denied security by the referee in the bankruptcy proceeding, but allowed as general claims. The Circuit Court, in anticipation of questions not before it, refused to determine the questions presented on the appeal, and, on a record in which no issue had been formulated with respect to any equities between different classes of creditors, and though the subordinated creditors had no opportunity to be heard, nevertheless subordinated the claims of certain creditors to respondents on equitable considerations which the court believed to have grown out of the prior reorganization proceedings.

The practical and inequitable effect of the decision is to penalize other creditors by giving to respondents a priority in payment (without defining its nature or basis) more extensive in its application to the assets of the bankrupt than respondents ever claimed to have on any theory of the case, in that it extends the priority to personal as well as real property, whereas the priority claimed by respondents under the reorganization plan was limited to real property.

STATEMENT OF FACTS

The bankrupt and a subsidiary (which is not concerned in or in any manner affected by this matter) filed a joint petition in reorganization on December 13, 1935. The bankrupt was in the general real estate investment business and as a part thereof borrowed and loaned money and conducted real estate loan, sales, and insurance departments (R. 3-11). Such petition was approved as properly filed (R. 11-13) and a Referee and Special Master was appointed (R. 14-15). Thereafter, such proceedings were had before the Referee and Court as resulted in the filing of an amended plan of reorganization (pamphlet pp. 1-12, shown in the record at p. 17), which provided for the payment of certain specified secured claims, taxes and expenses of administration, and classified the unsecured creditors into two groups described in Sections VIII and IX, such classifica-

tion being subject to later determination by the court of rank, disallowance of claims, further audit, and offsets (pamphlet pp. 5-7). All proposals contained in the amended plan were subject to such orders of reclamation and orders relating to foreclosure and/or sale as might be made by court or judge (pamphlet p. 7).

The amended plan was in due course accepted by the necessary number and amount of creditors; thereafter an amendment dated November 23, 1936 (R. 18-21) was proposed by the bankrupt (then debtor) modifying in certain respects Sections VIII and IX, which was approved by the court as a modification of the amended plan not materially adverse to the interests of any creditor or stockholder; and on April 2, 1937, the amended plan dated August 1, 1936, as thus modified was confirmed by the court (R. 21-26). Certain pertinent reservations were contained in the order of confirmation including the right to order the estate liquidated for failure to consummate the plan (R. 25).

Claims were filed with the referee and special master pursuant to law and the orders of court, among them the claims of respondents (R. 45-49).

On April 17, 1939, after notice to creditors and others interested pursuant to Chapter X, Article XI, Sections 222 and 223 of the Chandler Act, as required by the order of the Court, a further amendment granted an additional six months for consummation (R. 26-29). In the meantime, $8,775.75 principal and $2,717.27 interest, as provided by the plan, had been paid to the creditors whose claims totalling $35,275.83 had been classified in Section VIII, and other payments had been made to creditors holding liens, to discharge tax liens, and for costs of administration and expenses of continued operation of the business, all as provided by the plan and authorized by the court (R. 30-32).

On October 6, 1939, the bankrupt (then debtor) and its trustee filed a Report and Petition for Entry of Order of

Adjudication Pursuant to Chapter X, Article XII of the Bankruptcy Act (R. 29-34). Notice to show cause thereon was given pursuant to appropriate order of court, the pertinent part of such notice being as follows:

> "It is ordered: That the debtor, stockholders and creditors of The Mutual Investment and Security Company, as well as all other parties in interest, show cause at a hearing to be had on such petition before the District Court of the United States for the District of Colorado, at Denver, in said district, on the 25th day of October, 1939, at ten o'clock A.M. or as soon thereafter as such hearing may be had, why an order adjudging the debtor a bankrupt and directing that bankruptcy be proceeded with pursuant to the provisions of Article XII, Chapter X, of the Bankruptcy Act, should not be entered.
>
> "That notice of such hearing be given by mailing a copy of this order at least ten days prior to the date set for such hearing to each of the stockholders, creditors, and parties in interest entitled to notice of proceedings herein, and by publishing a copy thereof in The Daily Journal, at least once, more than ten days prior to the date set for such hearing" (R. 35).

After some continuances, the order of adjudication in bankruptcy was entered on December 12, 1939 (R. 36), no appeal was taken, and subsequently petitioner was duly appointed as trustee in bankruptcy of the bankrupt corporation.

On February 6, 1940, new secured claims were filed by respondents in the office of the referee to whom the matter had been previously referred. All such claims were identical except as to names and amounts, and were substantially as follows:

> "At Denver, in the State of Colorado, came Catherine J. Hanna, whose address is c/o A. J. Gould,

Midland Savings Building, in Denver County, State of Colorado, District of Colorado, and made oath and says that The Mutual Investment and Security Company, the corporation for which a petition for adjudication of bankruptcy has been filed, was at and before the filing of said petition and still is justly and truly indebted to said deponent in the sum of Sixteen Hundred Four Dollars and twenty-seven cents; plus interest at the rate of 4% per annum subsequent to April 2, 1939;

"That the consideration of said debt is as follows:

"This proceeding was instituted on the 13th day of December, 1935, by the filing herein, with the approval by this Honorable Court, of a petition of the debtor to be reorganized pursuant to the provisions of Section 77B of the Bankruptcy Statutes of the United States; that thereafter, and on the 12th day of August, 1936, the debtor filed herein an 'Amended Plan of Reorganization' and on the 7th day of December, 1936, the debtor filed a 'Proposed Amendment' to said 'Amended Plan of Reorganization'.

"That on or about the 2nd day of April, 1937, this Honorable Court, following proper notice to all interested persons, entered an order confirming said 'Amended Plan of Reorganization' as amended on December 7, 1936, by said 'proposed Amendment'.

"That by virtue of the provisions of said Section 77B, said 'Order of Confirmation' became a judgment of this court and all rights, liens and priorities of all of the debtor's creditors herein were finally determined and established thereby; that a certified copy of said 'Order of Confirmation' thereupon was recorded in the recorder's office of the City and County of Denver, Colorado.

"That by the terms of said 'Order of Confirmation'

and the provisions of the amended 'Amended Plan of Reorganization' this deponent was granted a general lien (with others described in Paragraph VIII of said 'Amended Plan') upon all of the debtor's interest in all of the real property of the debtor for the sum of $2139.03 which was therein determined to be due deponent with interest thereon at 4% per annum.

"That the trustee appointed by said 'Order of Confirmation' for the purpose of assisting in the execution of said plan and pursuant thereto, has paid deponent the sum of $534.76 on account of said principal amount and has paid interest thereon to deponent to April 2, 1939.

"That the sum of $1604.27 with interest thereon at 4% per annum subsequent to April 2, 1939, remains unpaid to deponent and is secured as hereinabove alleged.

"That said 'Amended Plan of Reorganization,' said 'Proposed Amendment' and said 'Order of Confirmation' are a part of the files in this proceeding and reference thereto is hereby made for greater certainty.

* * * *

"That no part of said debt has been paid nor are there any setoffs or counterclaims to the same except as appear from and upon the said exhibit . . . hereto attached; and that no note has been received for said debt and no judgment rendered thereon except as herein stated.

"That deponent has not, nor has any person by his order or to his knowledge or belief; for his use, had or received any manner of security for said debt whatever, except (describe fully).

* * * * *

"That said claim is not a preferred claim except for $....." (R. 62-64.)

Objections were filed by the trustee to each of such claims, substantially as follows:

"Comes now Earle F. Wingren, trustee duly appointed, qualified, and acting of the above named bankruptcy estate, and objects to the allowance of the claim of Catherine J. Hanna, numbered 60B, heretofore filed herein, as follows:

"Denies that the said claim is a secured claim, and alleges that the same is a general claim, and should be allowed and classified for payment in accordance with Section 64 of the Bankruptcy Act.

"Denies that by virtue of the provisions of Section 77B, the 'Order of Confirmation' entered in proceedings No. 8729 for the reorganization of corporations was a judgment and denies that all rights, liens, and priorities of all of the debtor's (the bankrupt's) creditors herein were finally determined and established thereby.

"Alleges that pursuant to the provisions of Section 77B (k) of the Bankruptcy Act, and to the provisions of Article XII of Chapter X of the so-called Chandler Act, said claim should be allowed and classified for payment in accordance with Section 64 of the Bankruptcy Act." (R. 61-62.)

No testimony was taken (R. 64); after hearing and argument the referee and special master handed down his findings and decision denying the claims of appellants as secured claims (R. 44-59). Petitions for review were filed (R. 59-60), and the record on review (R. 41-43) certified to the judge according to the praecipes filed by the parties pursuant to local rule of the District Court (R. 157).

Hearing was had before the District Court on the question certified which was as follows:

"Bankruptcy was preceded by a proceeding to reorganize under 77B. A plan was filed and confirmed. Subsequently the debtor was adjudicated a bankrupt. Claimants under reorganization claim the order confirming the plan was an adjudication of a priority in their favor which must be recognized in the bankruptcy proceeding instead of Section 64 of the Bankruptcy Act.

"Is the order of confirmation a final judgment establishing creditors' rights to distribution in bankruptcy even though in conflict with Section 64?" (R. 44.)

and the order of the referee confirmed (R. 64-65).

Thereafter notice of appeal was filed (R. 65); subsequently respondents (then appellants) filed a designation of contents of record on appeal (R. 66-67), which included items which had not been considered or noticed by either the referee or district judge, and none of which had been requested of or certified by the referee on petition for review (R. 41-43). Motion was filed by the trustee to submit the record on appeal to the District Court (R. 69) and after argument order was entered by the court excluding the items objected to (R. 71). No appeal was taken from such order, but thereafter respondents perfected their appeal to the Circuit Court of Appeals for the Tenth Circuit from the other order of the District Court confirming the referee on the main question.

No preliminary hearing was applied for in the Circuit Court with respect to the extent of the record or otherwise pursuant to District Court Rule 75 (j), and no certiorari for diminution of the record was applied for pursuant to Rule 13 of the Rules of the Tenth Circuit. The designation of points to be relied upon required by Rule 13 made no reference to the order of the district judge whereby the desired documents were excluded from the record (R. 1-2). Appellants in their first brief "suggested" a diminution of the record (R. 79), and attached to such

brief as an appendix the five documents expressly excluded from the record by the district judge (R. 117-129).

In due course the cause appealed was argued and submitted.

The Circuit Court of Appeals thereafter filed its opinion, holding that it was unnecessary to determine the questions raised by the parties and decided by the referee and district judge with respect to the nature and effect of the order of confirmation, and the necessarily related questions as to whether the confirmed plan was a contract, and if it was, whether it might be impaired by exercise of the bankruptcy power; whether respondents had any lien or priority, when and how it arose, and whether it was subject to the implied condition that the bankruptcy law might be changed; what effect Section 77B (k) and Chapter X, Article XII, Sections 236 and 238 had on the priority of debts; whether Section 77B (g) provided that a plan once confirmed, even though not consummated, should be binding on questions of classification of creditors; whether respondents had any vested rights of any kind, and other incidental questions. Instead, the court decided, citing *Pepper* vs. *Litton*, 308 U. S. 295, 84 L. Ed. 281, and *Taylor* vs. *Standard Gas & Elec Co.*, 306 U. S. 307, 83 L. Ed. 669, that "equitable considerations" required the claims of creditors of the class included in Section IX to be subordinated.

Thereafter, the Circuit Court entered its judgment, reversing the judgment of the District Court and remanding the cause for further proceedings consistent with the opinion of the court, and granting costs to respondents. Petitioner filed a petition for rehearing in said cause (R. 207-209), together with a brief in support thereof (R. 210-218), which petition was subsequently denied.

II.

JURISDICTION

The date of the judgment to be reviewed is July 19, 1941

(R. 204); rehearing was denied on August 25, 1941 (R. 219).

The statutory provision which is believed to sustain the jurisdiction of this court is the act of February 13, 1925, Chapter 229, Section 1, 43 Stat. 938, being Section 240 of the Judicial Code, as amended (28 U. S. C. A. 347) wherein it is provided that it shall be competent for the Supreme Court of the United States to review by certiorari a judgment of a Circuit Court of Appeals.

The nature of the case as disclosed from the summary statement and statement of facts hereinabove; the rulings of the court with respect to important questions of federal bankruptcy law, and the departure from the accepted and usual course of judicial proceedings are believed sufficient to warrant the exercise of judicial discretion by this court pursuant to the provisions of Rule 38 (5) of the rules of the United States Supreme Court.

Cases believed to sustain the jurisdiction are cited below with the reasons relied upon for granting the writ.

III.

QUESTIONS PRESENTED

The questions and propositions of law involved in this case are substantially as follows:

1. Can an appellate court depart from the issues and change a proceeding to consider the allowance of secured claims to a proceeding to adjust equities on order of distribution, especially where no issues have been formed and no evidence taken between respondents and other creditors, and it is by no means certain that all the evidence which other creditors might produce is in the record?

2. Does a bankruptcy court have the power to create a priority in payment not granted by statute upon any considerations of equity which may appeal to it in a particular case?

3. Does a bankruptcy court have the power to rest a decision in a particular case on general principles of equity applicable in bankruptcy proceedings if the exercise of such power amounts to a denial of applicable statutory provisions; i. e., Section 77B (k) (11 U.S.C.A. 207) and Chapter X, Article XII, Section 238 (11 U.S.C.A. 638), whereby Section 64 (11 U.S.C.A. 104) is made mandatory?

4. If a bankruptcy court has such power, did the facts and circumstances of the present case warrant its exercise to the extent that the result was to give to one group of creditors a priority in payment more extensive in its application to the assets of the bankrupt than such creditors could have enjoyed under the prior reorganization plan upon which they based their right, and greater than they have at any time contended for?

5. In a case where the respondents were before the court in a controversy with the trustee in bankruptcy involving the existence of a lien arising from the terms of a preceding confirmed but not fully consummated plan of reorganization and the court refuses to determine whether such lien exists, do any equitable considerations require or permit, in the decision of such controversy, the subordination to respondents' claims of the claims of other creditors, where the record is devoid of evidence of any legal relations between the two groups of creditors, or of any control over or activity in the affairs of the bankrupt, or of the reorganization proceedings, except that the required number of each group of creditors agreed to the plan of reorganization proposed by the company, and where the record is also devoid of any evidence of fraud, conduct involving moral turpitude, intention to deceive, or neglect or breach of duty on the part of such subordinated creditors, or any of them?

6. In a case where the claims of respondents, together with those of other creditors, were classified for payment under Section VIII of the plan of reorganization later con-

firmed, and such creditors were paid twenty-five per cent of their claims plus interest pursuant to such plan, where subsequently the plan failed, an order of adjudication was entered pursuant to Chapter X, Article XII (11 U.S.C.A. 636), of the Bankruptcy Act, and respondents thereafter within the period provided by Section 238 (11 U.S.C.A. 638) filed new secured claims for the balances owing to them based upon the terms of the confirmed but not consummated plan, without amendment of or reference to their original claims, have they elected to abandon the theory of their original claims and to rely only upon the new secured claims voluntarily filed by them?

7. Did respondents have any vested rights under the bankruptcy act or otherwise, either as preferred or lien creditors, prior to the order of confirmation?

8. If respondents had no vested rights prior to the order of confirmation, did their assertion that a trust relationship existed, taken together with the fact that the required two-thirds of each group of creditors consented to the plan, warrant the circuit court in the exercise of equitable powers, in giving respondents any priority on distribution of assets over the claims of simple contract creditors?

9. Did respondents acquire any vested rights of lien or otherwise, by virtue of the plan, the confirmed plan, or the order of confirmation, either as a contract or as a judgment; or did any such rights vest by express statute upon entry of the order of confirmation?

10. What is the nature and effect of the order of confirmation under Section 77B (f), (g), and (h) (11 U.S.C.A. 207)?

11. What is the nature and effect on the rights of creditors, of this plan of reorganization confirmed under Section 77B (11 U.S.C.A. 207)?

12. Where a petition asking for adjudication pursuant

to the provisions of Chapter X, Article XII (11 U.S.C.A. 636), of the Chandler Act is filed by the debtor, notices are sent to all interested persons pursuant to Section 236 (2) to show cause why the petition should not be granted, no cause is shown, the adjudication order is entered on the petition, and no appeal from that order taken, does the Chandler Act apply to the pending proceeding, is its application res adjudicata, and is the application of the particular provisions of Article XII to the subsequent conduct of the proceeding mandatory?

13. If the Chandler Act does apply to this proceeding, what is the meaning and effect of Chapter X, Article XI, Sections 222, 223, 224 and 228 (11 U.S.C.A. 622-4, 628), in so far as they relate to the revocation or modification of an order of confirmation entered under Section 77B; and of Chapter X, Article XII, Sections 236 and 238 (11 U.S.C.A. 636, 638), in so far as they relate to the rights of persons whose claims as creditors were classified for the purposes of a plan of reorganization initiated under Section 77B?

14. Does usual and accepted judicial practice permit the enlargement of a record on appeal to the Circuit Court by inclusion therein by appendix to appellants' brief (R. 117-127) of material not noticed or considered by the Referee or District Judge, consisting of five separate documents, four of which (R. 117-122) were never made a part of the files in the District Court either by certification to the court of the record on review by the Referee, or otherwise?

15. Does Rule 75(h) of the Rules of Civil Procedure for the District Courts permit the District Court on proper submission of the record to it, to exclude from the record on appeal material not noticed or considered either by Referee or Judge?

16. Does the Circuit Court of Appeals have the right under Rule 75(h) of the Rules of Civil Procedure, on sug-

gestion for the first time made in appellants' brief, or on its own initiative, to consider as a part of the record on appeal material expressly ordered (R. 69) to be excluded from that record by the District Court after hearing under Rule 75 (h), but thereafter appended to appellants' brief as an appendix, where there has been no previous application to the Circuit Court for an intermediate order or for certiorari under Rule 13 of the Rules of the Tenth Circuit, and where there has been no appeal from the order of the District Court excluding such material from the record?

IV.

REASONS RELIED ON FOR ALLOWANCE OF WRIT OF CERTIORARI

The reasons relied on for the allowance of the writ are as follows:

1. The novelty of the questions presented and the great importance of the provisions of the reorganization sections of the Bankruptcy Act to the business world and to the legal profession, as well as to the courts charged with the administration of the Bankruptcy Act, require an authoritative and elucidating decision, particularly as to those sections which relate to the nature and effect of orders of confirmation of plans of reorganization, and the status and rights of creditors in the case of confirmed plans only partially consummated and followed by bankruptcy or liquidation. In the following cases certiorari has been granted because of the importance of the questions involved.

Palmer v. *Conn. Ry & L. Co.*, dec. Jan. 6, 1941, 85 L. Ed. Adv. Op. No. 5, p. 283.

Wright v. *Union Cent. L. I. Co.*, dec. Dec. 9, 1940, 85 L. Ed. Adv. Op. No. 3, p. 166.

Cons. Rock Prod. Co. v. *DuBois*, dec. Mar. 3, 1941, 85 L. Ed. Adv. Op. No. 9, p. 603.

Sampsell v. *Imperial Paper & C. Corp.*, dec. Apr. 28, 1941, 85 L. Ed. Adv. Op. No. 13, p. 797.

Palmer v. *Webster & Atlas Nat. Bank*, dec. Feb. 3, 1941, 85 L. Ed. Adv. Op. No. 7, p. 436.

Woods v. *City Nat. B. & T. Co.*, dec. Feb. 3, 1941, 85 L. Ed. Adv. Op. No. 7, p. 478.

Palmer v. *Massachusetts*, 308 U. S. 79, 84 L. Ed. 93.

Hancock Mutual Life Ins. Co. v. *Bartels*, 308 U. S. 180, 84 L. Ed. 176.

Carpenter v. *Wabash Ry. Co.*, 309 U. S. 23, 84 L. Ed. 558.

Thompson v. *Magnolia Pet. Co.*, 309 U. S. 478, 84 L. Ed. 876.

Union Joint Stock Land Bank v. *Byerly*, 310 U. S. 1, 84 L. Ed. 1041.

Sec. & Exch. Com. v. *U. S. R. & Impt. Co.*, 310 U. S. 434, 84 L. Ed. 1293.

In *Carpenter* v. *Wabash*, 309 U. S. 23, 84 L. Ed. 558, certiorari was granted in view of the importance of an amendment relating to the priority of certain claims.

2. The questions of federal law with respect to the status and rights of creditors in a bankruptcy proceeding following the failure of a partially consummated plan of reorganization have not been, but should be, settled by this court. In the following case certiorari was granted to decide a bankruptcy question not previously settled by the Supreme Court.

Fisher v. *Pauline O. & Gas. Co.*, 309 U. S. 294, 84 L. Ed. 764.

3. The decision of the said Circuit Court of Appeals in expressly refusing to apply to respondents' claims the provisions of the amendatory act (Chapter X, Article XII, Secs. 236 and 238, 11 U. S. C. A. 636, 638) is an erroneous decision of an important question of bankruptcy law, and is in conflict with a decision of the Circuit Court for the Third Circuit, i. e., *In re Columbia Ribbon Co.*, 117 Fed. (2d) 999, wherein the precise point was decided, and is in substantial conflict with a decision of the Circuit Court for

the Second Circuit; i. e., *In re Carden*, 118 Fed. (2d) 677, wherein an amendatory provision of the Chandler Act was found to be mandatory, and applied to the exclusion of equitable considerations. In the following case certiorari has been granted where such a conflict existed.

Thompson v. *Magnolia Pet. Co.*, 309 U. S. 478, 84 L. Ed. 876.

4. The decision of the Circuit Court of Appeals was based on the supposed authority of the decisions of the court in *Pepper* v. *Litton*, 308 U. S. 295, 84 L. Ed. 281, and *Taylor* v. *Standard Gas & Elec. Co.*, 306 U. S. 307, 83 L. Ed. 669, but the questions presented by and involved in the case of petitioner were not, as petitioner believes, presented by or involved in either *Pepper* v. *Litton* or *Taylor* v. *Standard Gas & Elec. Co.*, and the said questions raised here were not decided in either of those cases, nor were the same necessary for the determination of either of those cases. Rule 38, 5 (b), Revised Rules of the United States Supreme Court.

5. The decision of the Circuit Court of Appeals as to the application of "equitable considerations" and its refusal to consider the pertinent statutory provisions is the decision of questions of federal law in conflict with principles established by applicable decisions of this court wherein limitations on the exercise of equitable powers have been consistently recognized, as in *Sec. & Exch. Com.* v. *U. S. R. & Imp. Co.*, 310 U. S. 434, 84 L. Ed. 1293, 1303, and cases therein cited, and in *U. S. Rubber Co.* v. *American Oak L. Co.*, 181 U. S. 434, 45 L. Ed. 938. In the following case certiorari was granted because of such conflict:

Ansaldo San Giorgio v. *Rheinstrom Bros.*, 294 U. S. 494, 79 L. Ed. 1016, 1019.

6. The decision of the Circuit Court in refusing to determine the legal effect of the order of confirmation and of the confirmed plan, is in conflict with principles established by this court in *Meyer* v. *Kenmore Granville Hotel Co.*, 297 U. S. 160, 80 L. Ed. 557, wherein the nature of an order confirming a plan was settled. The Tenth Circuit has

heretofore recognized such case as authority in *In re Deep Rock Oil Corp.*, 113 Fed. (2d) 266, 269, with specific reference to the possibility of modification of a confirmed plan.

Ansaldo San Giorgio v. *Rheinstrom Bros.*, supra.

7. The decision of the said Circuit Corut of Appeals, in holding that equitable considerations govern the instant case, although the record contains no facts tending to support such application, so far departs from the accepted and usual course of judicial determination as to call for the exercise of the supervisory powers of the Supreme Court in bankruptcy matters. Rule 38 (b), Revised Rules of the United States Supreme Court.

8. The decision of the Circuit Court of Appeals in holding that the claims of the Section IX creditors be subordinated, amounts to a finding of fact that the subordinated creditors were guilty of some inequitable conduct, without any evidence to support such finding, was erroneous as a matter of law, and hence within the scope of review of this court.

Lawson v. *U. S. Min. Co.*, 207 U. S. 1, 52 L. Ed. 65, 74.

Chicago, Milw. & S. P. Ry. v. *Coogan*, 271 U. S. 472, 70 L. Ed. 1041, 1044.

Panama Mail Ss. Co. v. *Vargas*, 281 U. S. 670, 74 L. Ed. 1105.

9. The importance of the procedural problem in administration of the Bankruptcy Act. The decision of the Circuit Court of Appeals, in ignoring the questions raised by the parties as to enlargement of the record on appeal after it had reached the Circuit Court of Appeals (by means of appending material not considered by the referee or district judge as an appendix to appellants' first brief) tacitly approves irregularities in practice which so far depart from the accepted and usual course of judicial proceedings with respect to records on review and appeal as to require the determination by this court of the propriety of such practice, and an authoritative decision as to the powers of both

the District Courts and the Circuit Courts under Rule 75, and especially the power of the District Court to make a record conform to the truth under paragraph (h) of such Rules.

Reconstruction Finance Corp v. *Prudence Sec. Adv. Group*, dec. Jan. 6, 1941, 85 L. Ed. Adv. Op. No. 5, p. 300.

Duke Power Co. v. *Greenwood*, 299 U. S. 259, 81 L. Ed. 179.

Wherefore, your petitioner prays that a writ of certiorari issue under the seal of this court, directed to the Circuit Court of Appeals for the Tenth Circuit, commanding said court to certify and send to this court a full and complete transcript of the record and of the proceedings of the said Circuit Court had in the case numbered and entitled on its docket, No. 2245, Minnie C. Hanssen, et al., Appellants, vs. Earle F. Wingren, Trustee in Bankruptcy of The Mutual Investment and Security Company, Appellee, to the end that this cause may be reviewed and determined by this court as provided for by the statutes of the United States and the Rules of this court; and that the judgment of said Circuit Court be reversed by the court, and for such further relief as to this court may seem proper.

Dated at Denver, Colorado, September 30, 1941.

EARLE F. WINGREN, Trustee in Bankruptcy of The Mutual Investment and Security Company,

Petitioner,

By NORMA L. COMSTOCK,

Counsel for Petitioner.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

OPINIONS OF COURT BELOW.

The opinion in the Circuit Court (R. 200-204) dated July 18, 1941, appears in 121 Fed. (2d) Adv. Op. No. 5, page 1011.

II.

GROUNDS OF JURISDICTION.

The date of the judgment to be reviewed is July 19, 1941 (R. 204); petition for rehearing was denied August 25, 1941 (R. 219).

Jurisdiction is invoked under Section 240 of the Judicial Code, 28 U. S. C. A. 347. Writ of certiorari is sought on the following grounds:

(1) That the Circuit Court of Appeals has decided important questions of federal law which have not been, but should be, settled by this court;

(2) That said Court has decided federal questions of law in a way probably in conflict with applicable decisions of this court;

(3) That said court has rendered a decision in conflict with the decision of another Circuit Court of Appeals in respect to the mandatory application of the Chandler Act;

(4) That said court has so far departed from the accepted and usual course of judicial proceedings, both in respect to procedural matters governed by Rule 75 of the Rules of Civil Procedure for the District Court, relating to appeals, and in respect to the court's consideration of alleged facts and circumstances calling for the exercise of its equitable power, where such circumstances do not appear from the record on appeal, as to call for an exercise of this court's power of supervision; and

(5) The grave importance of the questions involved in this cause to the orderly administration of the Bankruptcy Act.

Citations of cases wherein certiorari has been granted on these grounds have been cited in the preceding petition under IV, pages 14-18, and are hereby adopted and reference made a part of this brief.

III.

STATEMENT OF THE CASE.

In this case bankruptcy was preceded by a reorganization proceeding under Section 77B. A plan was filed, confirmed, partially consummated, and then failed. Subsequently the debtor was adjudicated a bankrupt on a petition expressly praying for adjudication under Chapter X, Article XII, of the Chandler Act. The order of adjudication was not appealed. Respondents claimed the order confirming the plan was an adjudication in their favor of security which must be recognized in the subsequent bankruptcy proceeding instead of Section 64 of the Act. The Referee and District Court denied the security and allowed respondents' claims as general unsecured creditors (R. 59, 65). The Circuit Court expressly refused to decide the questions thus raised by the parties, and on equitable considerations, subordinated the claims of other creditors to those of respondents, with the practical result that respondents gained a priority even greater than they claimed to have under the plan.

The action of the court in basing its decision on equitable principles, had the effect of changing a proceeding to hear and determine the validity of secured claims to a proceeding to adjust equities on order of distribution.

The present controversy arose between the respondents and the trustee upon the hearing of respondents' secured claims, filed under Chapter X, Article XII, Section 238 (3) (R. 62-64) and the trustee's objections to such claims as secured (R. 61-62). No controversy between the respondents and general creditors was raised by the issues, nor was there any question before referee or judge as to rights of priority on order of distribution, the proceeding not hav-

ing progressed to the point where distribution was imminent.

In arriving at its conclusion, the court obviously considered as part of the record on appeal certain material not a part of the record on appeal, but appended to appellants' first brief as an appendix (R. 117-127), and as a result clearly misconceived the nature of the respective rights of the two classes of creditors as they existed prior to the confirmation of the plan.

A chronological factual statement of the case has been stated in the preceding petition under I, pages 1-9, and is hereby adopted by reference and made a part of this brief.

IV.

SPECIFICATION OF ERRORS INTENDED TO BE URGED.

1. The circuit court had no power in the circumstances of this case to create, on equitable considerations, a priority in payment not granted by statute, and the attempted exercise of such power in this case constituted a departure from the issues formed in a proceeding to consider the allowance of secured claims to a proceeding to adjust equities on order of distribution, wherein no issue had been formed and no evidence taken between respondents and other creditors; and also constituted a forfeiture of the just debts of those creditors not before the court.

2. The attempted exercise by the circuit court of its power to adjust equities between creditors upon the payment of dividends on order of distribution, constitutes an express denial of the applicable statutory provisions; i. e., Section 77B (k) (11 U. S. C. A. 207 (k)), and Chapter X, Article XII, Section 238 (11 U. S. C. A. 638), whereby Section 64 (11 U. S. C. A. 104) applies.

3. If the circuit court did have power in this controversy between trustee and respondents as secured claimants, to adjust equities between general creditors as if on order of distribution, the exercise of such power in this case was unwarranted, unjust, and inequitable. in that the result was to penalize Section IX creditors by granting to the class of creditors to which respondents belong, a priority in payment more extensive in its application to the assets of the bankrupt than could have been enjoyed by such creditors had the plan been fully consummated.

4. If the circuit court did have power, in this controversy between trustee and respondents as secured claimants, to adjust equities between general creditors as if on order of distribution, there were no facts or circumstances shown by the record, or otherwise, sufficient in law or in

equity, to require or permit the exercise by a court of equity of such power.

5. The court erred in its conclusion that the mere assertion by respondents that a trust relationship had existed between them and the bankrupt company entitled them to the special consideration of the court as a court of equity, and wholly overlooked the fact that respondents had elected to abandon the trust theory of priority by filing new secured claims based on the order of confirmation.

6. The court, though expressly refusing to determine whether a contract existed between the parties, obviously based its decision largely upon the consent of the subordinated creditors to the plan of reorganization by which respondents were granted a priority in payment; stated otherwise, the court held that the subordinated creditors were estopped to deny the priority. The court erred in finding, by inference, that an estoppel can be based on a contract which has been abrogated.

7. The court erred in refusing to determine the following specific questions raised by the parties:

(a) Whether respondents had any vested rights as preferred or priority creditors prior to the order of confirmation,

(b) Whether the order of confirmation was but a step in the reorganization proceedings, subject to modification and revocation, or was a judgment finally adjudicating the rights of all creditors.

(c) Whether the confirmed plan was a contract binding upon the creditors for all purposes, either under the provisions of Section 77B (g) (11 U. S. C. A. 207 (g)), or otherwise.

(d) Whether any lien existed in favor of respondents by virtue of the plan, the confirmed plan, the order of confirmation, or by express statute upon entry of the order of confirmation.

(e) Whether upon the entry of an order of adjudication expressly requested pursuant to the provisions of Chapter X, Article XII, which order of adjudication was not appealed, the application of said chapter and article are res adjudicata, and the application of Section 64 was mandatory or discretionary.

(f) Whether in the circumstances of this case, if the provisions of the Chandler Act are not applicable, whether Section 77B (k) is applicable and whether the application of said Section 64 is then mandatory or discretionary.

8. The court erred in refusing to decide the questions raised with respect to the enlargement of the record on appeal and in considering the appendix to appellants' first brief as a part of the record on appeal after the documents therein shown were excluded from the record.

V.
SUMMARY OF THE ARGUMENT

I. THE CIRCUIT COURT OF APPEALS HAD NO POWER IN THIS PROCEEDING TO GRANT A PRIORITY OR TO SUBORDINATE CREDITORS ON EQUITABLE CONSIDERATIONS.

(a) The Circuit Court is an appellate court and as such lacks power to depart from the issues formed below to consider equities between persons not parties to the proceedings.

(b) The Circuit Court had no greater power in any event than that possessed by a bankruptcy court, which itself has no power to create a priority or preference in payment.

(c) The exercise of equitable powers was an express denial of applicable statutory provisions.

(d) The attempt of the court to adjust equities between general creditors was unjust and inequitable in its result, and imposed a penalty on the subordinated creditors.

(e) There are no facts and circumstances in this case sufficient in law or equity to permit the exercise of the power to adjust equities, and the mere assertion of a trust relationship does not entitle respondents to special equitable consideration.

(f) Estoppel cannot be based on a contract which has been abrogated.

II. A. RESPONDENTS HAD NO VESTED RIGHT ENTITLING THEM TO PRIORITY IN PAYMENT ON ANY THEORY.

(1) Prior to the order of confirmation, because

(i) They were not secured or lien creditors and had established no priority on the trust fund theory; and

(ii) There are no vested rights in priorities under a bankruptcy act.

(2) By virtue of the order of confirmation as a judgment, because

(i) The order of confirmation in a reorganization proceeding is not the final order, as in a composition;

(ii) It is binding only in a limited sense, being subject to modification and vacation, and is only a step in the reorganization proceedings;

(iii) The court retains jurisdiction of the proceedings after entry of order of confirmation for purposes of supervision as well as other purpurposes;

(iv) Allowance of all claims in bankruptcy is subject to reconsideration and reclassification.

(3) By virtue of the confirmed plan as a contract, because

(i) The debtor had no power to make a binding contract under the circumstances;

(ii) Any contract which exists is wholly dependent upon the bankruptcy law;

(iii) Any exercise of the bankruptcy power by Congress impairs the obligation of contracts, and such impairment is not itself a denial of due process; and

(iv) Any contractual right is subject to the implied condition that the bankruptcy law may be amended or repealed.

(4) The lien claimed under the contract was subject to the same qualifications and limitations as the contract itself.

B. APPLICABILITY AND EFFECT OF THE CHANDLER ACT.

(1) It is res adjudicata.

(2) The application of Section 64 under Chapter X, Section 238, is mandatory.

III. THE COURT ERRED IN FAILING TO DECIDE THE PROCEDURAL QUESTIONS.

ARGUMENT.

I.

THE CIRCUIT COURT OF APPEALS HAD NO POWER IN THIS PROCEEDING TO GRANT A PRIORITY OR TO SUBORDINATE CREDITORS ON EQUITABLE CONSIDERATIONS.

(a) *The Circuit Court is an appellate court and as such lacks power to depart from the issues formed below to consider equities between persons not parties to the proceedings.*

The opinion of the Circuit Court reads in part as follows:

> "The appellants have provable claims within the purview of Section 63 of the Bankruptcy Act is attested by the fact that the referee allowed their claims. He denied them any lien or priority. Other-

wise stated, he decided that the claims of creditors included in Section IX of the plan should be allowed as on a parity with the claims of creditors included in Section VIII of the plan. We think this was error, and that equitable considerations require the claims of creditors of the class included in Section IX of the plan be subordinated." (R. 203.)

That respondents have provable claims under Section 63 is not denied, nor is it denied that the referee's denial to them of any lien or priority is equivalent to a finding that the claims of both classes of creditors should be allowed on a parity; the Circuit Court also found, by inference, that both classes are general creditors. But it does not follow that the referee decided that both classes should be paid equal dividends on distribution. That question was not before him, nor was it before the District Court, nor has it been submitted to the appellate jurisdiction of the Circuit Court.

Circuit courts are appellate courts; (11 U.S.C.A. 1 (3) exercising appellate jurisdiction (11 U.S.C.A. 47); district courts are courts of bankruptcy (11 U.S.C.A. 1 (10)) exercising equitable jurisdiction (11 U.S.C.A. 11).

Questions of equities between persons not parties to the proceedings in the bankruptcy court, and not presented to or ruled on by that court are not to be decided by the circuit court, as in bankruptcy proceedings its jurisdiction is purely appellate.

> *Amick* v. *Columbia Cas. Co.*, 101 Fed. (2d) 984 (8th Cir. 1939).

The Circuit Court could not in this proceeding accord priority to respondents' claims and such an order would in effect determine the ultimate rights between respondents and each of the subordinated creditors. Such evidence as appears from the record may be admissible in a later proceeding, but it is far from certain that all the evidence which the parties might be entitled to produce is to be found in the present record.

Davis v. *Louisville Trust Co.*, 181 Fed. 10 (6th Cir. 1910).

Mesker v. *Ohio Riv. Sand Co.*, 285 Fed. 379 (6th Cir. 1922).

The adjustment of equities between creditors on order of distribution, where the issues are properly formed and evidence taken on the respective rights of the general creditors, or some of them, was not the proceeding before the circuit court on appeal. The decision of that court is an improper attempt by an appellate court to act as a court of bankruptcy and to exercise the equitable powers of courts of bankruptcy.

This controversy arose on the hearing before the referee of the allowance of secured claims wherein respondents contended that they were secured by virtue of an order of confirmation entered in the preceding reorganization proceeding (R. 62-64). The trustee denied the validity of the security but admitted the existence of the claims as general claims (R. 61-62). No notice of the hearing on the claims was given to other creditors. Some of the Section IX creditors voluntarily appeared by attorneys, but took no part in the proceeding except upon the argument of the law. No testimony was offered by the respondents or the trustee and no opportunity for offering testimony was given to those general creditors who were represented. Innumerable other general creditors had no notice of the original proceeding nor were they represented at any of the hearings before the referee, district court or circuit court.

The statement of points relied on by appellants (R. 1-2) filed pursuant to Rule 13 of the Revised Rules of the Tenth Circuit (See Appendix E to this brief) raised no questions of equities between creditors, and the circuit court, by its own rule, should limit its consideration to the points so stated.

(b) *The Circuit Court had no greater power in any event than that possessed by a bankruptcy court, which itself*

has no power to create a priority or preference in payment.

The word "priority" does not refer to liens existing on the bankrupt's property, nor to the order of payment of such liens, but to the order of payment out of the general assets of an insolvent's estate on distribution after satisfaction of valid liens. Where the creditor, before the bankruptcy, has an established lien on the bankrupt's property which is not invalidated by the bankruptcy, he is a secured creditor.

6 *Remington on Bkcy.*, 4th Ed., Sec. 2839, p. 417.
Dallas v. *Ryan*, 62 Fed. (2d) 959 (5th Cir. 1933).

It is well settled that a bankruptcy court has no power to grant a priority or preference in payment because of any considerations which may appeal to it as falling within general principles of equity distribution. *So. Bell Tel. & Tel. Co.* v. *Caldwell*, 67 Fed. (2d) 802 (8th Cir. 1933), and *In re Columbia Ribbon Co.*, 117 Fed. (2d) 909 (3rd Cir. 1941).

The bankruptcy act prescribes a certain order of priority in the payment of creditors out of the net amount of the fund left after separation of property belonging to adverse claimants and lienholders, which order of priority has no reference to lien debts.

Lott v. *Salisbury*, 237 Fed. 191 (4th Cir. 1916).
Burton Coal Co. v. *Franklin Coal Co.*, 67 Fed. (2d) 796 (8th Cir. 1933).
6 *Remington on Bankruptcy*, 4th Ed., Sec. 2778, pp. 329, 330.

The power of a bankruptcy court in an appropriate proceeding to adjust equities among general creditors in the order of distribution by postponing payment of one group to payment of others is not denied, but such power must be carefully distinguished from the efforts to create a priority on equitable principles not granted by statute, in a case where the controversy arose between alleged secured creditors and the trustee as to the validity of the security.

6 *Remington on Bankruptcy*, 4th Ed., Sec. 2875, pp. 477, 483.

(c) *Exercise of equitable powers was an express denial of applicable statutory provisions.*

That the bankruptcy act requires the separation of property belonging to others, and that secured by valid lien, from the net fund to be administered for the benefit of creditors is settled. Section 64 (11 U.S.C.A. 104—see appendix C to this brief) demands the payment of creditors in a certain specified way. Assuming that under the provisions of Section 77B (k) (11 U.S.C.A. 207(k)—see Appendix B to this brief) there might have existed a right in respondents to have the court exercise in liquidation proceedings some discretionary power in the classification of claims in conformity with an equitable receivership under the equity powers of the court as in *In re Ostlind Mfg. Co.*, 19 Fed. Sup. 836 (Ore. 1937), and *In re Collins Hosiery Mills*, 18 Fed. Sup. 90 (Pa. 1937), that privilege has been expressly withdrawn by the adoption of the amendatory act, Section 238 of Chapter X (11 U.S.C.A. 638—see Appendix A to this brief). The omission in the later act of the words found in Section 77B(c)(8) (11 U.S.C.A. 207(c)(8)) "direct the estate to be liquidated" manifested congressional intent to deprive creditors of any right which they might have formerly enjoyed to have the estate liquidated in any other manner than under Section 238, whereby Section 64 is mandatory. Equitable principles may govern action in a bankruptcy court when not in conflict with the statute, but where there has been an amendment to the statute whereby such right formerly existed, there has been the equivalent of a statutory denial of the right, and any action under general principles of equity contrary thereto would be contrary to the statute and so erroneous.

In re Columbia Ribbon Co., 117 Fed. (2d) 999 (3rd Cir. 1941).

In re Carden, 118 Fed. (2d) 677 (3rd Cir. 1941).

Equitable doctrines will apply except as they are inconsistent with the act.

Local Loan Co. v. *Hunt*, 292 U. S. 234, 78 L. Ed. 1230.

Pepper v. *Litton*, 308 U. S. 295, 84 L. Ed. 281.

Securities & Exch. Com. v. *U. S. R. & Imp. Co.*, 310 U. S. 434, 84 L. Ed. 1293.

In re Columbia Ribbon Co., 119 Fed. (2d) 999 (3rd Cir. 1941).

In re Pacific Oil & Meal Co., 24 Fed. Sup. 767, 771 (D. C. Cal.).

(d) *Attempt of court to adjust equities between general creditors was unjust and inequitable in its result, and imposed a penalty on the subordinated creditors.*

Assuming that the circuit court had the power to adjust equities in this controversy, the exercise of the power by subordination of all the creditors included in Section IX to all those included in Section VIII resulted in penalizing the Section IX creditors by unjustly granting to Section VIII creditors a priority more extensive than they might have enjoyed had the plan been fully consummated. In effect, the court found that, by reason of the former proceedings in reorganization, Section VIII creditors should be allowed to keep the $11,523.00 which they have already received (R. 32), and should in addition be paid the remainder of their claims from the proceeds of all the bankrupt's real and personal property, instead of being paid merely from the proceeds of the bankrupt's real property and the income therefrom, to which they alleged they were entitled under the plan (R. 19). While this record does not show what the practical result may be, as the controversy arose before a distribution was imminent, it is apparent that under the circuit court's ruling none of the fund available for distribution may ever reach the Section IX creditors. It follows, therefore, that although they are not before the court, they have been penalized for the trustee's objection to the allowance of respondents' claims as secured claims. In such a case a court of equity should not declare a forfeiture of just debts, or, by postponing them

till all other creditors are satisfied, practically confiscate them.

U. S. Rubber Co. v. *American Oak Leather Co.*, 181 U. S. 434, 447-448, 452-453; 45 L. Ed. 938, 946, 948.

Wells v. *Lincoln*, 214 Fed. 227 (9th Cir. 1914).

Keppel v. *Tiffin Sav. Bank*, 197 U. S. 356, 49 L. Ed. 790.

(e) *There are no facts and circumstances in this case sufficient in law or equity to permit the exercise of the power to adjust equities and the mere assertion of a trust relationship does not entitle respondents to special equitable consideration.*

Assuming that in a proceeding of this kind, where no such issues have been formulated and presented as to enable the court to determine the rights of respondents against other creditors, or any of them, the record (including the purpose of this portion of the argument the material excluded by the district judge from the record on appeal (R. 117-127), is nevertheless devoid of any evidence tending to bring the subordinated creditors within the principles established by the Supreme Court and other circuit courts in cases wherein subordination has been properly ordered.

Pepper v. *Litton*, 308 U. S. 295, 84 L. Ed. 281, and *Taylor* v. *Standard Gas & Elec. Co.*, 306 U. S. 307, 83 L. Ed. 669, are cited by the circuit court as authority for subordination on equitable considerations. Careful examination of both cases discloses no circumstances comparable to this case.

In *Pepper* v. *Litton*, the question was properly up for decision by the circuit court on appeal. (See L. Ed., pp. 284-285.) Therein the claim of a dominant stockholder who had failed in his duty to the corporation, and had sought an unjust advantage, was subordinated. It was held that a bankruptcy court has power to inquire into the validity of any claim asserted against the estate and to disallow it if it is ascertained to be without lawful existence. It was *not* held that the court had the power to inquire into the

validity of one claim, and on that inquiry to disallow or subordinate other claims not before it (U. S. Rep., p. 305, L. Ed. 288). The entire inquiry in *Pepper* v. *Litton* relates to the disallowance or subordination on equitable principles of claims of persons who as directors or dominant or controlling stockholders have asserted an improper measrue of control over the affairs of the corporation prior to bankruptcy and whose claims must be tested by the fiduciary relationship existing between themselves and the corporation. In that case the record fairly reeked with the fraud and scheming of the claimant.

In *Taylor* v. *Standard Gas & Elec. Co.* the same principles were applied to test the claims of a parent corporation against its subsidiary, and the claims of the parent were subordinated to the claims of preferred stockholders of the subsidiary because of the history of spoliation, mismanagement, and faithless stewardship of the affairs of the fiduciary by the parent.

Bird and Son Sales Corp. v. *Tobin*, 78 Fed. (2d) 371 (8th Cir. 1935), 100 A.L.R. 654, involved the construction of Section 65a (11 U.S.C.A. 105(a)), in the light of Sections 1 and 2 (11 U.S.C.A. 1 and 11). In that case an agreement was made among certain creditors providing that in consideration of the granting of additional credit to the bankrupt company, some would agree, in the event of liquidation, to subordinate their claims to those who advanced additional credit. The court held that the contract entered into among the creditors prior to bankruptcy should be enforced. The question was raised upon the recommendations of the trustee to the referee in making the order of distribution. Due notice was given to all creditors who had filed claims (see 100 A.L.R. 655); the referee upon hearing of the trustee's suggestions adopted them and ordered the dividend to creditors who had signed the agreement to be withheld and distributed pro rata to the subsequent creditors whose indebtedness as above stated accrued subsequent to the execution of the agreement and in reliance thereupon. The District Court approved the order of the

referee and the Circuit Court of Appeals affirmed the District Court. The decision was correct. A bankruptcy court has power to adjudicate equities arising out of the relation of the general creditors with one another when the issues are formed and after due notice has been given to all creditors on the order of distribution. Following the report of this case in the American Law Reports (p. 660) is an annotation with respect to the power of a bankruptcy court to adjudicate equities among creditors in distribution of dividends. The distinction between adjustment of equities among creditors and the creation of priorities not granted by statute clearly appears from the cases therein noted.

In this case there is no evidence whatever of any legal relations, contractual or otherwise, between the two groups of creditors or any of them prior to the filing of the petition in reorganization, nor of any control over or activity in the affairs of the bankrupt company by the subordinated creditors, or any of them, either prior to filing of the petition in reorganization or since. The petition in reorganization was filed by the company, the amendments were proposed by the company, the modifications approved by the court were proposed by the company, and finally the petition asking for adjudication under Section 236, Chapter X (11 U.S.C.A. 636) was filed by the company. None of the subordinated creditors are responsible for the mismanagement of the company prior to filing of the petition, nor for either progress or failure of the proceedings subsequent thereto. Their only connection with the matter was that the required number of their group consented to the plan of reorganization proposed by the company and acquiesced in the modifications and in the order of adjudication. Respondents did likewise.

The record is also devoid of any evidence of fraud, conduct involving moral turpitude, intention to deceive, or any neglect or breach of duty on the part of such subordinated creditors or any of them, either to the respondents or to any other creditors. *Crowder* v. *Allen-West Com. Co.*, 213 Fed. 177 (8th Cir. 1914.)

The circuit court in its opinion, which for the purposes of this case must be taken to be its findings of fact, recited certain conclusions which it apparently drew from the record on appeal and the material excluded from the record but attached to respondents' first brief (R. 117-127) and from statements in that brief which are outside the record. There was no testimony before the court to form a basis for any such conclusions and at least some of them are entirely without foundation in the record. It is not denied, as stated by the circuit court, that at the time the petition was initiated respondents might have been able to establish a right to priority in payment on the trust fund theory by showing augmentation of the debtor's assets and had they succeeded in doing so certain valuable rights would have accrued to them. They might have been able to reclaim their property or money, in which event such property or money would never have become a part of the bankruptcy estate to be administered. The court states that some of these rights were or may have been lost by their acceptance of the plan. There is nothing in the record to show that any such rights were lost—in fact, had they desired to do so, they might have pressed petitions for reclamation of their funds or property under the express provisions of Section X of the plan (R. 17, pamphlet p. 7). If inferences are to be drawn from the consent of any creditor or group of creditors to the plan proposed, then the fair inference to be drawn from the consent of respondents to the proposed plan of reorganization is that they consented that their claims be paid subsequent to secured claims and expenses of administration and other priority claims mentioned in Sections I-VII of the plan (R. 17, pp. 1-5), but prior to the creditors mentioned in Section IX, because they thereby gained a priority in payment which they otherwise could not establish. Stated differently, it can be safely assumed that had they been able to trace funds and thereby remove such funds from the administration of the bankruptcy court, they would certainly have done so.

The mere assertion that a trust relationship existed between respondents and the bankrupt company did not en-

title them to any priority in payment or to any equitable consideration by the bankruptcy court.

Schuyler v. *Littlefield*, 232 U. S. 707, 58 L. Ed. 710.
In re Rosenbaum Iron Corp., 112 Fed. (2d) 315 (7th Cir. 1940).

However, it follows that since in bankruptcy all of the provisions relating to allowance of claims become applicable, that respondents still have a right to establish their rights to priority on the trust fund theory if they choose to do so, unless indeed, they have abandoned the right so to proceed by filing in the subsequent bankruptcy proceeding their new secured claims wherein no amendment of their former claims was attempted or any reference made to their prior status.

The impossibility of placing respondents in statu quo is admitted, and in that connection the fact (ignored by the court) that respondents have already received $11,523 is significant. Certainly the debtors' financial position was different on the date of adjudication from its position on the date of confirmation of the plan. Neither can Section IX creditors be placed in statu quo. Any knowledge of the possibility of failure in the consummation of the plan with which Section IX creditors are charged must also be charged to respondents as they knew equally as much of the facts and of the possible weaknesses of the plan. There is no question here involved where one group of creditors or one creditor misled others or misinformed others, and the respondents at all times had knowledge equal in extent to that possessed by the subordinated creditors.

Whatever the bankrupt may have done in violation of its legal duty to respondents, the subordinated creditors are not responsible for or bound by the consequences, and they constitute no basis of estoppel as to them. *In re Bowman Hdw. & Elec. Co.*, 67 Fed. (2d) 792 (7th Cir. 1933).

(f) *Estoppel cannot be based on a contract which has been abrogated.*

The court, though expressly refusing to decide whether

any contract existed, either under the order confirming the plan or irrespective of statute (R. 201-202) held, by inference, that an estoppel against Section IX creditors arose therefrom. This question has previously been carefully considered by the Tenth Circuit in *U. S.* v. *Golden*, 34 Fed. (2d) 367, 373, wherein it was held that, although where one has contracted in the light of certain facts, ordinarily he is estopped to deny their existence, the estoppel exists only so long as the contract, and an estoppel cannot be based on a contract which has been abrogated. The contract here, if any existed, was abrogated by the subsequent adjudication in bankruptcy, an eventuality which all parties to the contract were fully aware might occur.

II.

None of the points of law above argued was presented to the circuit court, as the question of the equities claimed to exist between the two groups of creditors was not formed as to issues, and was never seriously argued in the briefs. Such argument as there was, was directed to alleged abuse of discretion in applying the Chandler Act to the proceedings, to the end that the security claimed by respondents by virtue of the order of confirmation be allowed to them.

It follows, therefore, that since the circuit court had no power to decide the question before it on equitable considerations, or to anticipate questions which might arise on order of distribution and payment of dividends, it devolved upon that court to determine the specific questions raised by the parties bearing on the allowance or denial of the security claimed by respondents. The argument following relates to those points:

A. RESPONDENTS HAD NO VESTED RIGHT ENTITLING THEM TO PRIORITY IN PAYMENT ON ANY THEORY.

(1) *Prior to Order of Confirmation:*

Respondents have never claimed to have any liens or rights as secured creditors, by way of judgment, statute,

contract, or otherwise, on the date of filing of the petition in reorganization. That is the date as of which their rights must be fixed, as priorities not then existent cannot later arise. This is true both as to the bankrupt and among the creditors. *U. S.* v. *Marxen,* 307 U. S. 200, 207, 83 L. Ed. 1222, 1228.

Neither did respondents have any vested rights in the assets of the bankrupt except their right to be paid out of such assets, which by the filing of the petition for reorganization became in *custodia legis,* and then constituted a fund sequestered for the benefit of creditors. The mere assertion by respondents that a trust relationship existed which entitled them to reclaim money or property, is not sufficient to secure to them a preferred status. The funds must be traced.

Schuyler v. *Littlefield,* 232 U. S. 707, 58 L. Ed. 710.
American Service Co. v. *Henderson,* 120 Fed. (2d) 525 (4th Cir. 1941).
Swan v. *Children's Home Society,* 67 Fed. (2d) 84, 88 (4th Cir. 1933).

If the creditor cannot trace his property he cannot reclaim no matter what the equities are. Instead he is relegated to the position of asserting his rights as a general creditor. *In re Rosenbaum Iron Corp.,* 112 Fed. (2) 315, 318 (7th Cir. 1940).

In any event, there is no vested right in priorities under a bankruptcy act. Changes in the existing law may be made in the remedy so long as they do not affect the right.

Kuehner v. *Irving Tr. Co.,* 299 U. S. 445, 81 L. Ed. 340.
Carpenter v. *Wabash,* 309 U. S. 23, 84 L. Ed. 558.
In re Old Algiers, Inc., 100 Fed. (2d) 374 (2nd Cir. 1938).
In re Prima, 88 Fed. (2d) 785 (7th Cir. 1937).
Chelsea v. *Dolan,* 24 Fed. (2d) 522 (1st Cir. 1928, cert. den. 72 L. Ed. 1012).

Thompson v. *Siratt*, 95 Fed. (2d) 214 (8th Cir. 1938).

In re Chi., R. I. & P. Co., 90 Fed. (2d) 312 (7th Cir. 1937, cert. den. 82 L. Ed. 554), 113 A.L.R. 487.

Adams v. *Bowen*, 46 Fed. (2d) 294 (1st Cir. 1931).

Inland Dredging Corp., 61 Fed. (2d) 765 (2nd Cir. 1932, cert. den. 77 L. Ed. 985); 88 A.L.R. 254.

(2) *By virtue of the order of confirmation as a judgment:*

Did respondents acquire any vested rights by virtue of the order of confirmation as a judgment which would carry over to the date of bankruptcy, December 12, 1939, and consequently be enforceable in the present proceeding?

Such was the question certified to the district court by the referee (R. 43-44). It involves determination of the nature and effect of the order of confirmation in the reorganization proceedings (R. 21-26), which necessarily requires first an examination into the nature of a reorganization proceeding itself.

The constitutionality of the reorganization amendments to the Bankruptcy Act has been upheld on the ground that they do no more than apply the principles of composition in a way found practicable in certain instances.

Continental Ill. Nat. B. & Trust Co. v. *Chicago, R. I. & P. R.R. Co.*, 79 L. Ed. 1111, 294 U. S. 648.

In re Central Funding Corp., 75 Fed. (2d) 256 (2nd Cir. 1935).

Campbell v. *Alleghany Corp.*, 75 Fed. (2d) 947, 952 (4th Cir. 1935, cert. den. 56 S. Ct. 72).

However, it does not follow that reorganization and composition are one and the same thing for all purposes. *Callaghan* v. *RFC*, 80 L. Ed. 805, 297 U. S. 464.

One of the most important points of difference between composition and reorganization is *when* the agreement is made binding. In composition, two steps must be taken before an application for confirmation of a composition may be filed: (1) acceptance must be procured in accord-

ance with the requirements of the act; (2) the consideration for the composition, whether money or property, must be deposited in the court subject to the order of the judge. Thereupon, the order of confirmation is entered, the bankrupt revested with title to his property, and discharged of his debts. Whether a particular creditor ever receives his consideration is of no moment—his rights are determined by the entry of the order of confirmation, which is the *final* order approving and rendering effective the proposed contract among the creditors and with the bankrupt. The bankrupt has no further duties toward his creditors—he has deposited his consideration—it is out of his control —he is free of his debts.

> *In re Laubheim Bros.*, 22 Fed. (2d) 910, 911, (2nd Cir. 1937).
>
> *In re J. B. Pollak Co.*, 86 Fed. (2d) 99, (2nd Cir. 1936).
>
> *Nassau Smelting & Ref. Co.* v. *Brightwood Bronze F. Co.*, 68 L. Ed. 1013, 265 U. S. 269.
>
> *Cumberland Glass Co.* v. *DeWitt*, 68 L. Ed. 1042, 237 U. S. 447.

The entry of the order of confirmation under Section 77B (g) (11 U.S.C.A. 207 (g)) was quite different. Such order was entered after acceptance of the plan and certain other preliminary provisions had been compiled with, whereupon the debtor had then to proceed to carry out the plan and the orders of the judge. It was not by the order of confirmation relieved of further obligations to its creditors nor to the court; it had not parted with any specified sum of money or parcel of property as the consideration for its discharge on confirmation of the proposed plan; it was still subject to certain obligations to consummate the plan proposed; upon fulfillment of such obligations, a report had to be made to the court, and then, and only then, a *final* order was entered closing the case and discharging the debtor from its debts, except as provided in the plan.

The nature of an order of confirmation has been considered by this court which decided as follows:

> "* * * an order confirming a plan of reorganization under Sec. 77B is not the equivalent of a judgment granting or denying a discharge, for unlike confirmation of a composition, see (July 1, 1898) Sec. 14, 30 Stat. at L. 544, 550, chap. 541, U.S.C.A. title 11, Section 32 (c) it does not operate as a discharge. The release of the debtor in a reorganization proceeding is contingent upon the performance of its part of the reorganization plan. Section 77B (h) commands the debtor and others to execute the plan of reorganization, when confirmed, under the direction of the court, authorizes the court to make appropriate orders to that end, and provides that 'upon the termination of the proceedings a final decree shall be entered,' which 'shall discharge the debtor from its debts and liabilities.' Discharge is effected not by confirmation of the plan but by the final decree." *Meyer* v. *Kenmore Granville Hotel Co.*, 80 L. Ed. 557, 560, 297 U. S. 160.

Upon confirmation in reorganization, the plan is said to be "binding upon all creditors" (Sec. 77B, subd. g), but this, of course, is subject to the right of subsequent modification of the plan (subd. f) upon proper notice and after opportunity is afforded for withdrawal of acceptance by any creditor who has previously accepted the plan. It is apparent, then, that the order of confirmation "binds" the creditors only in a limited sense, and that it is the final decree provided by subd. (h) that closes the case and finally fixes the rights of the parties.

The order of confirmation is but a step in the reorganization proceedings:

> *Meyer* v. *Kenmore Granville Hotel Co.*, 80 L. Ed. 557, 560; 297 U. S. 160
>
> *In re Eastern Utilities Inv. Corp.*, 98 Fed. (2d) 620, 623 (3rd Cir. 1938)

Wright v. *City Nat'l Bank*, 104 Fed. (2d) 285 (6th Cir. 1939)

Campbell v. *Allegheny Corp.* 75 Fed. (2d) 947, 955 (4th Cir. 1935)

and is not a final judgment fixing creditors' rights. The court of the Tenth Circuit has cited as authority two of the cases above mentioned, with specific reference to the possibility of subsequent modification of a confirmed plan. *In re Deep Rock Oil Corp.*, 113 Fed. (2d) 266, 269 (1940).

Possibility of modification is an important element to be considered as bearing on the nature of the order of confirmation. Such a modification of this plan was actually effected once (April 17, 1939, *after* the Chandler Act became effective, and pursuant to it), upon appropriate notice to creditors (R. 26-29). The provisions of both acts respecting modification are copied in appendices A and B to this brief.

Both Sections 77B and Chapter X of the Chandler Act clearly distinguish between confirmation and consummation. The word "consummation" is not used in Section 77B but the words "carry out" are used. Careful reading and comparison of the two acts show that the order of conrmation was never by either intended to fix the rights of the parties except subject to the carrying out, completion, or consummation of the plan of reorganization in accordance with its terms and the orders of the court. Both acts subject the debtor to the continued jurisdiction of the court, both acts direct proceedings in the same fashion as to the appointment of a trustee, filing and classification of claims, etc. *Wiggin Terminals* v. *Hassett*, 35 Fed. Sup. 654 (Mass. 1941).

In this case the district judge specifically reserved jurisdiction for many purposes in the order of confirmation, including the power to liquidate the estate in the event of the failure of the plan (R. 25), thereby intentionally limiting the binding effect of the order.

The distinction between preliminary or administrative orders and final decrees in reorganization proceedings has been consistently recognized:

National Lock Co. v. *Hogland*, 101 Fed. (2d) 576 (7th Cir. 1938)

In re Corona Radio and Television Corp., 102 Fed. (2d) 959 (7th Cir. 1939)

In re Paramount Publix Corp., 82 Fed. (2d) 230 (2nd Cir. 1936)

In re Mallow Hotel Corp., 29 Fed. Sup. 931 (Pa. 1939)

Mohonk Realty Corp. v. *Wise*, 111 Fed. (2d) 287 (2nd Cir. 1940).

The bankruptcy court can alter its administrative decrees in aid of creditors or of the debtor where no intervening rights of innocent third parties (of whom we have none here) have been or are likely to be materially interfered with, and could abrogate a rental purchase lease notwithstanding the fact that it had previously approved it. *In re Roger Williams Bldg. Corp.*, 99 Fed. (2d) 212 (7th Cir. 1938), cert. den. 59 S. Ct. 1032.

Section 57k of the Bankruptcy Act is applicable both under Section 77B and the Chandler Act. It specifically gives the bankruptcy court the power to reconsider claims, which power may be exercised *sua sponte*, upon the application of another creditor, the trustee, or even the bankrupt. This power to reconsider and reclassify claims is thoroughly recognized. *Pepper* v. *Litton*, 308 U. S. 295, 305, 84 L. Ed. 281, 288.

On the theory that the allowance of a claim in bankruptcy is a judgment, the allowance of respondents' claims for payment under Section VIII of the plan was subject to reconsideration and reclassification, in which event the law as it existed at the time of the reconsideration would apply. *U. S.* v. *Heinszen*, 206 U. S. 370, 51 L. Ed. 1098.

(3) *By Virtue of the Confirmed Plan as a Contract:*

Any contract right which may have arisen as of April 2, 1937, the date of confirmation of the plan, or prior thereto by virtue of the proposed plan and its acceptance, must necessarily be considered in the light of the bankruptcy law pursuant to which such contract, if any, was made. A corporation debtor which has subjected itself to the jurisdicetion of the court for the purpose of procuring a reorganization but which, as a result of its submission to jurisdiction, may suffer an adjudication in bankruptcy instead, cannot make any valid contracts with its creditors except in accordance with the statute and with the express consent of the court. *Case* v. *L. A. Lbr. Prod. Co.*, 84 L. Ed. 110, 126, 127, 308 U. S. 106. Hence, it follows that if any contract exists, it exists not irrespective of statute, but by virtue thereof.

Assuming, however, that a valid contract was created by virtue of the offer of the plan, its acceptance, and the entry of order of confirmation it was at all times subject to possible subsequent impairment by some exercise of the bankruptcy power, either pursuant to then existing statutes or pursuant to such amendatory acts as might by Congress be adopted.

Any exercise of the bankruptcy power impairs the obligation of contracts and such impairment is not itself a denial of due process.

> *Campbell* v. *Alleghany Corp.*, 75 Fed. (2d) 947, 953 (4th Cir. 1935, cert. den. 56 S. Ct. 92).
>
> *Kuehner* v. *Irving Trust Co.*, 299 U. S. 445, 81 L. Ed. 340.

> "No person has a vested interest in any rule of law entitling him to insist that it shall remain unchanged for his benefit. Munn v. Illinois, 94 U. S. 113, 134, 24 L. Ed. 77; New York Central R. Co. v. White, 243 U. S. 188, 198, 37 S. Ct. 247, 61 L. Ed. 667, L.R.A. 1917D, 1, Ann. Cas. 1917D, 629. . . . The leg-

islation being a proper exercise of the bankruptcy power, there is no merit in the objection it affects obligations incurred before its enactment. Canada Southern Ry. Co. v. Gebhard, 109 U. S. 527, 539, 3 S. Ct. 363, 27 L. Ed. 1020; Continental Illinois Nat. Bank v. Chicago, Rock Island & P. Ry. Co., 294 U. S. 648, 674, 55 S. Ct. 595, 605, 79 L. Ed. 1110; United States Nat. Bank v. Pamp, 8 Cir., 77 Fed. (2d) 9, 99 A.L.R. 1370; Campbell v. Alleghany Corp., 4th Cir., 75 Fed. (2d) 947." *Thompson* v. *Siratt*, 95 Fed. (2d) 214, 217, 218.

* * * * *

"All parties to a contract are, of necessity, aware of the existence of, and subject to, the power of Congress to legislate on the subject of bankruptcies. They were or are chargeable with knowledge that their rights and remedies, in case the debtor becomes insolvent and is adjudicated a bankrupt, are affected by existing bankruptcy laws and all future lawful bankruptcy legislation which might be enacted. The amendments to the bankruptcy laws were not therefore necessarily an unlawful impairment of the contractual rights of either party. All loans were made and all credit extended with the knowledge that the power to enact such laws existed and application of such legislation might alter the contractual rights of the creditor. To illustrate: A discharge in bankruptcy is the goal of the debtor in the ordinary bankruptcy proceedings, yet, a discharge of debts necessarily abridges the creditor's contract and his rights thereunder. *Another unavoidable conclusion is that all contracts are made with the knowledge that existing bankruptcy laws may be amended.*

". . . In fact, the entire bankruptcy act might be repealed and no vested right invaded." *In re Prima Co.*, 88 Fed. (2d) 785, 788 (7th Cir. 1937). (Italics ours.)

(4) *The lien claimed under the contract was subject to the same qualifications and limitations as the contract itself:*

If a lien was established by the contract approved by the order of confirmation, it was at all times subject to the limitations of the plan, the reservations in the order confirming it, and to the implied condition that the bankruptcy law might effect changes in its enforcement.

Kuehner v. *Irving Trust*, 299 U. S. 445, 81 L. Ed. 340.

Ginsberg v. *Lindel*, 107 Fed. (2d) 721 (8th Cir. 1939).

In re Chicago, R. I. & P. Co., 90 Fed. (2d) 312, 316, 113 A.L.R. 487 (7th Cir. 1937).

Such a lien was necessarily dependent upon the ability of the debtor to effectuate the whole plan, not merely a part of it; it was granted in contemplation of complete reorganization.

Failure of the court to determine whether any lien or security existed, and to define its nature, leaves undecided vital questions of interpretation of the reorganization sections of the bankruptcy act, properly raised in this proceeding, the determination of which is necessary to the proper administration of the estate, upon which the Supreme Court has not as yet expressed its views.

B. APPLICABILITY AND EFFECT OF THE CHANDLER ACT.

(1) *Its applicability is res adjudicata:*

The petition for adjudication was filed pursuant to the provisions of Chapter X, Article XII, of the Chandler Act. By filing such petition the debtor took advantage of procedure thus made available to it which possibly had not before existed. All persons in interest were notified, and although no written response was made to the show cause order (R. 35) "after several postponements the matter came on for hearing on December 12, 1939, and upon full

hearing" (R. 39) the order was entered. No appeal was taken and the question of the applicability of the Chandler Act to the pending proceeding is res adjudicata. It was expressly made applicable by the order of adjudication which by its terms is based on the petition requesting adjudication under Article XII of the Chandler Act (R. 36).

No question of abuse of discretion by the district judge in rendering this particular provision of the Chandler Act applicable to the pending reorganization proceeding is open to argument, the order not having been appealed from. Therefore, there is no question of applicability under Article XVI, Section 276c, of the Chandler Act; the remaining question is as to the *effect* that the order of adjudication has on such rights, if any, as may have been acquired in the reorganization proceeding (R. 39-41).

(2) *The application of Section 64 is mandatory:*

So far as effect is concerned, analysis of Section 77B establishes that appellants had no greater or different rights under that amendatory act than they have under the present Chandler Act, also amendatory.

Section 77B (a) (11 U.S.C.A. 207(a)) provided, among other things, that upon the approval of the filing of a petition the court should during the pendency of the proceedings have exclusive jurisdiction of the debtor and its property and "shall have and may exercise all the powers, not inconsistent with this section, which a federal court would have had it appointed a receiver in equity of the property of the debtor by reason of its inability to pay its debts as they mature." Chapter X, Article III, Section 115 (11 U. S. C. A. 515), is substantially identical.

Section 77B (c) (8) provided that if a plan was not proposed and accepted, or not confirmed, the judge might, after hearing, extend the period, dismiss the proceeding, or direct the estate to be liquidated, which liquidation would have to proceed as in Section 77B (k), which pro-

vided, among other things, that "debts *shall* be entitled to priority as provided in Section 64." Certain other sections of the bankruptcy act relating to appointment of trustee, etc., were especially made applicable, and "the date of the order approving the petition or answer under this section shall be taken to be the date of adjudication, and such order shall have the same consequences and effect as an order of adjudication." Chapter X, Article XII, Sec. 236(2), and Sec. 238 (11 U.S.C.A. 636, 638) are substantially identical, except that the words "or if a confirmed plan is not consummated" have been added. The general method of procedure prescribed for the future administration of the estate is the same, whether it is called "liquidation" in the first act, or "procedure in bankruptcy" in the second. The same provision is retained as to the effective date of the "adjudication," except that in the latter act the effect is qualified by the substitution of "shall as far as possible" for "shall" in Section 77B.

The application of the provisions of Section 238 is mandatory in a situation where reorganization has failed.

In re Columbia Ribbon Co., 117 Fed. (2d) 999 (3rd Cir. 1041).

In re Calif. Pea Pro. Co., 37 Fed. Sup. 659, 661 (Cal. 1941).

In re Centralia Ref. Co., 35 Fed. Sup. 599, 601-2 (Ill. 1940).

Hi-Flier Mfg. Co. v. *Haberman*, 115 Fed. (2d) 918 (2nd Cir. 1940)

Under Section 77B there might have been two methods of liquidation. *In re Ostlind Mfg. Co.*, 19 Fed. Sup. 836 (Ore. 1937) proceedings were had in conformity with an equitable receivership rather than in accord with Section 77B (k). The court expressly disapproved the procedure.

In re Collins Hosiery Mills, Inc., 18 Fed. Sup. 90 (Pa. 1937), contains an analysis of the manner of liquidation under Section 77B which the court considered open to the judge. The conclusion was that two methods were available: (1) liquidation under the equitable powers of the court;

and (2) a liquidation under creditor control following the procedure set forth in subdivision (k). The court says the liquidation under (1) should take place only where exceptional circumstances demand it.

Chapter X, Article XII, Section 238 (11 U.S.C.A. 638), deprives the court of the first method of liquidation.

Application of Section 64 under 77B (k) is mandatory.

In re Manhattan Music Hall, 14 Fed. Sup. 48 (N. Y. 1936).

Miners Sav. Bank v. *Joyce*, 97 Fed. (2) 973 (3rd Cir. 1938).

In re Higgin Mfg. Corp., 19 Fed. Sup. 120 (Ky. 1937).

Application of Section 64 under Chapter X, Article XII, Section 238, involves no exercise of discretion of the court because of the use of the words "so far as possible." "Possible" does not mean the same thing as "practicable." *In re Kenilworth Bldg. Corp.*, 105 Fed. (2d) 673, 676 (7th Cir. 1939). It is possible to apply Section 64 to the payment to creditors of funds arising from assets of the bankrupt corporation which are still in the hands of the trustee, and there is no question of practicability here. Compare *In re Manhattan Music Hall*, 14 Fed. Sup. 48, 52, and *In re Old Algiers*, 100 Fed. (2d) 374 (2nd Cir. 1938).

It should also be noted that Section 238 (3) absolutely limits the claims which shall be provable to those provided by Section 63, which would naturally have the effect in some cases of denying any participation whatever to creditors in the subsequent bankruptcy proceedings on account of claims which might have been proved and allowed for payment in a plan confirmed in a prior reorganization proceeding. Congress allowed no discretion to the court to determine what was either practicable or possible in the application of Section 63, and it follows that it intended no discretion to exist as to Section 64. Section 238 is explicit and mandatory and the court has no discretion to act con-

trary to its terms. Compare *Carpenter* v. *Wabash*, 309 U. S. 23, 84 L. Ed. 558.

III.

THE COURT ERRED IN FAILING TO DECIDE THE PROCEDURAL QUESTIONS

Respondents in their Designation of Record on Appeal filed in the district court (R. 66-67), included the material which they have appended to their brief as an appendix (pp. i-xi) (R. 117-127). The four papers which they have thus attempted to include in the record to be sent to this court were not considered by the referee, were not certified by him to the district court, and were not considered by the district court on petition for review, as is apparent from the referee's Record on Petition for Review (R. 41-43) and from Motion for Submission of Record on Appeal to the District Court (R. 69). The first four of such papers relating to the particular claims of Minnie C. Hanssen and Thyra H. Mankin (R. 66, Items 4, 6, 7, and 8) were not filed in the office of the clerk of the district court but were part of the files in the office of the referee, as appears from the certified copies thereof (R. 117-122). There is nothing in the referee's opinion (R. 44-59) to indicate that the referee considered these documents, though he does (R. 45-46) describe the *claims* filed by these particular creditors.

The trustee's motion to settle the question of whether such papers should be included in the record on appeal (R. 69) was filed on the theory that respondents were attempting to enlarge the record by bringing to the attention of the circuit court material not included in the record on review and not considered by the district judge.

The bankruptcy rules of this district provide:

> "Petitions for review of all orders of the referee shall be accompanied by a praecipe setting out in detail the record to be sent up for review, including a statement of the evidence desired to be sent up, and all exhibits, books, and other documents re-

quired to be sent; and petitioner shall at that time or such time as he may be notified by the referee of the amount of costs required, pay for making such record, transcript or documents." Rules of the U. S. Dist. Court, District of Colo., Rule 13, Sec. 1.

Such rules, adopted pursuant to General Order No. 37 and Rule 83 of the Rules of Civil Procedure, where not inconsistent with the Bankruptcy Act, the General Orders and the Rules of Civil Procedure, have the effect of law.

Weil v. *Nary*. 278 U. S. 160, 73 L. Ed. 243, 249.
Bronx Brass Foundry, Inc., v. *Irving Trust Company*, 297 U. S. 230, 80 L. Ed. 657.

Rule 75(h) of the Rules of Civil Procedure provides that while it is not necessary for the record on appeal to be approved by the district court or judge, if any difference arises *as to whether the record truly discloses what occurred in the district court*, the difference shall be submitted to the court and *the record made to conform to the truth*. Logically, this must mean that the judge may exclude from the designated record on appeal any pleadings, documents, transcript or other material which is actually not a part of the record in his court.

At the time the matter was brought up to the district court from the referee on petition for review, the respondents themselves did not regard as relevant the material which they later presented as an appendix to their brief. If every appellant in a bankruptcy matter were permitted, after having his contentions denied by the district court on petition for review, to reach back into the files of the referee and extract therefrom such additional matter as he believed might improve his case on appeal to the circuit court, right of review by the district court would be destroyed and there would be no point in requiring litigants to have their controversies heard by the district court before presentation to the circuit court of appeals. What was appealed to the circuit court was the order of the district court and the record was the record of the district court. As a matter of practice, if appellants are entitled to sup-

plement their record from the referee's office, then appellees would be entitled to the same privilege, and the result would be new cases in the circuit made up from the files of the referee.

The trustee also objected to the inclusion of these documents in record on appeal because Items 4, 6, 7, and 8 relate only to one of the claims from the disallowance of which this appeal is taken. He denies that such documents accurately reflect the facts with respect to the claims of *all* of the respondents, nor of the claims of *all* of the Section VIII creditors. Respondents are not all of such creditors; they represent the majority in amount, but not the majority in number R. 31-32).

The power of the district court to determine such questions has been affirmed in the only case directly touching on the point, wherein it was stated that that court could better determine the facts than the circuit court. *Reynolds* v. *Imlay*, 118 Fed. (2d) 53 (C.C.A., D. C., 1941).

No motion for an intermediate order touching this matter was made in the circuit court by respondents, nor was certiorari for diminution of the record sought. See Rule 75 (h) and (j), Rules of Civil Procedure for the District Courts, and Rule 13 of the Revised Rules of the Tenth Circuit, appended hereto as an appendix at pages 62-63.

Addition to the record on appeal of the documents described tended to confuse the record, and raised in the circuit court a basis of claim which was not mentioned in the claims as filed (R. 62-63). The nature and status of respondents' original claims sufficiently appear from the findings and decision of the referee (R. 45-46).

The circuit court obviously considered the excluded material in arriving at its conclusions with respect to the equities which it has stated existed in favor of respondents, with the result that it has greatly exceeded its powers as an appellate court in subordinating certain creditors in a

proceeding initiated solely to determine the allowance of secured claims.

We ask that a writ of certiorari be granted and that upon final hearing the judgment of the circuit court be reversed.

Respectfully submitted,

JOHN W. SHIREMAN,
NORMA L. COMSTOCK,
NORMAN H. COMSTOCK.

Denver, Colo., Sept. 30, 1941.

APPENDIX A.

CHAPTER X.

ARTICLE XI.

Sec. 222. A plan may be altered or modified, with the approval of the judge, after its submission for acceptance and before or after its confirmation if, in the opinion of the judge, the alteration or modification does not materially and adversely affect the interests of creditors or stockholders. If the judge finds that the proposed alteration or modification, filed with his approval, does materially and adversely affect the interests of creditors or stockholders, he shall fix a hearing for the consideration, and a subsequent time for the acceptance or rejection, of such alteration or modification. The requirements in regard to notice of hearing, to submission to the Securities and Exchange Commission, to acceptance, to filing and hearing of objections to confirmation and to the confirmation, as prescribed in article VII of this chapter in regard to the plan proposed to be altered or modified, shall be complied with. (11 U. S. C. A. 622.)

Sec. 223. Any creditor or stockholder who has previously accepted the plan proposed to be altered or modified and who does not file a written rejection of the proposed alteration or modification within the time fixed by the judge, shall be deemed to have accepted the alteration or modication and the plan so altered or modified unless the previous acceptance provides otherwise. (11 U. S. C. A. 623.)

Sec. 224. Upon confirmation of a plan—

(1) The plan and its provisions shall be binding upon the debtor, upon every other corporation issuing securities or acquiring property under the plan, and upon all creditors and stockholders, whether or not such creditors and stockholders are affected by the plan or have accepted it or have filed proofs of their claims or interests and whether or not their claims or interests have been scheduled or allowed or are allowable. (11 U. S. C. A. 624 (1).)

Sec. 228. Upon the consummation of the plan, the judge shall enter a final decree—

(1) Discharging the debtor from all its debts and liabilities and terminating all rights and interests of stockholders of the debtor, except as provided in the plan or in the order confirming the plan or in the order directing or authorizing the transfer or retention of property:

(2) Discharging the trustee, if any;

(3) Making such provisions by way of injunction or otherwise as may be equitable; and

(4) Closing the estate. (11 U. S. C. A. 628.)

ARTICLE XII.

Sec. 236. If no plan is proposed within the time fixed or extended by the judge, or if no plan proposed is approved by the judge and no further time is granted for the proposal of a plan, or if no plan approved by the judge is accepted within the time fixed or extended by the judge, or if confirmation of the plan is refused, or if a confirmed plan is not consummated, the judge shall—

(1) Where the petition was filed under section 127 of this Act, enter an order dismissing the proceeding under this chapter and directing that the bankruptcy be proceeded with pursuant to the provisions of this Act; or

(2) Where the petition was filed under section 128 of this Act, after hearing upon notice to the debtor, stockholders, creditors, indenture trustees, and such other persons as the judge may designate, enter an order either adjudging the debtor a bankrupt and directing that bankruptcy be proceeded with pursuant to the provisions of this Act, or dismissing the proceeding under this chapter, as in the opinion of the judge may be in the interests of the creditors and stockholders. (11 U. S. C. A. 236.)

Sec. 238. Upon the entry of an order directing that bankruptcy be proceeded with—

(1) Where the petition was filed under section 127 of this Act, the bankruptcy proceeding shall be deemed reinstated and shall thereafter be conducted, so far as possible, as if the petition under this chapter had not been filed; or where the petition was filed under section 128 of this Act, the proceeding shall thereafter be conducted so far as possible, in the same manner and with like effect as if an involuntary petition for adjudication had been filed at the time when the petition under this chapter was filed, and a decree of adjudication had been entered at the time when the petition under this chapter was approved;

(2) A trustee shall be appointed pursuant to section 44 of this Act and shall supersede any trustee previously appointed; and

(3) Only such claims as are provable under section 63 of this Act shall be allowed, and claims not already filed may be filed prior to the expiration of three months after the first date set for the first meeting of creditors as provided in section 55 of this Act, or, if such date has been previously set, then prior to the expiration of three months after the mailing of notices to creditors of the entry of the order directing that bankruptcy be proceeded with. (11 U. S. C. A. 638.)

APPENDIX B.

Section 77B

(c) * * * (8) if a plan of reorganization is not proposed or accepted within such reasonable period as the judge may fix, or, if proposed and accepted, is not confirmed, may, after hearing, whether the proceeding be voluntary or involuntary, either extend such period or dismiss the proceeding under this section or, except in the case of a railroad or other public utility or of a debtor which has not been found by the judge to be insolvent, direct the estate to be liquidated, or direct the trustee or trustees to liquidate the estate, appointing a trustee or trustees if none shall previously have been appointed, as the interests of the creditors and stockholders may equitably require; * * *." (11 U. S. C. A. 207 (c) (8).)

(f) * * * Before or after a plan is confirmed, changes and modifications may be proposed therein by any party in interest and may be made with the approval of the judge after hearing upon notice to creditors and stockholders, subject to the right of any creditor or stockholder who shall previously have accepted the plan to withdraw his acceptance, within a period to be fixed by the judge and after such notice as the judge may direct, if, in the opinion of the judge, the change or modification will be materially adverse to the interest of such creditor or stockholder, and if any creditor or stockholder having such right of withdrawal shall not withdraw within such period, he shall be deemed to have accepted the plan as changed or modified: *Provided, however,* That the plan as changed or modified shall comply with the provisions of subdivision (b) of this section and shall have been or shall thereafter be accepted as required by the provisions of subdivision (e), clause (1), of this section, including acceptances by reason of failure to withdraw as hereinbefore provided, and the provisions of this subdivision (f), and of subdivision (e), clause (2), of this section, shall have been complied with in respect thereof. (11 U. S. C. A. 207 (f).)

(g) Upon such confirmation the provisions of the plan and of the order of confirmation shall be binding upon (1) the debtor, (2) all stockholders thereof, including those who have not, as well as those who have, accepted it, and (3) all creditors, secured or unsecured, whether or not affected by the plan, and whether or not their claims shall have been filed, and, if filed, whether or not approved, including creditors who have not, as well as those who have, accepted it. (11 U.S.C.A. 207 (g).)

(h) Upon final confirmation of the plan, the debtor and other corporation or corporations organized or to be organized for the purpose of carrying out the plan, shall have full power and authority to, and shall put into effect and carry out the plan and the orders of the judge relative thereto, under and subject to the supervision and control of the judge, and the property dealt with by the plan, when transferred and conveyed by the trustee or trustees to the debtor or the other corporation or corporations provided for by the plan, or, if no trustee has been appointed, when retained by the debtor pursuant to the plan or transferred by it to the other corporation or corporations provided for by the plan, shall be free and clear of all claims of the debtor, its stockholders and creditors, except such as may consistently with the provisions of the plan be reserved in the order confirming the plan or directing such transfer and conveyance or retention, and the court may direct the trustee or trustees, or if there be no trustee, the debtor and any mortgagee, the trustee of any obligation of the debtor, and all other proper and necessary parties, to make any such transfer or conveyance, and may direct the debtor to join in any such transfer or conveyance made by the trustee or trustees. Upon the termination of the proceedings a final decree shall be entered discharging the trustee or trustees, if any, making such provisions as may be equitable, by way of injunction or otherwise, and closing the case. Such final decree shall discharge the debtor from its debts and liabilities, and shall terminate and end all rights and interests of its stockholders, except

as provided in the plan or as may be reserved as aforesaid. * * * (11 U. S. C. A. 207 (h).)

(k) If an order is entered directing the trustee or trustees to liquidate the estate pursuant to the provisions of clause (8) of subdivision (c) of this section: (1) The case may be referred to a referee as provided in section 22, who shall be compensated as provided in section 40; (2) the first meeting of creditors shall be held as provided in section 55, upon notice as provided in section 58; (3) a trustee or trustees shall be appointed as provided in section 44, and be compensated as provided in section 48; (4) claims which are provable under section 63 may be proved as provided in section 57, except that the time within which proof may be made shall not expire until six months after the date of the last publication of the notice of the first meeting; (5) debts shall be entitled to priority as provided in section 64; (6) sales shall be made as provided in subdivision (b) of section 70; (7) dividends may be declared and paid as provided in section 65. None of the sections enumerated in this subdivision (k) except subdivisions (g), (i), (j), and (m) of section 57 of this title, and subdivisions (a) and (e) of section 70 of this title, shall apply to proceedings instituted under this section 77B unless and until an order has been entered directing the trustee or trustees to liquidate the estate. All other provisions of this Act, except such as are inconsistent with the provisions of this section 77B, shall apply to proceedings instituted under this section, whether or not an order to liquidate the estate has been entered. For the purposes of such application, provisions relating to "bankrupts" shall be deemed to relate also to "debtors"; "bankruptcy proceedings" or "proceedings in bankruptcy" shall be deemed to include proceedings under this section; the date of the order approving the petition or answer under this section shall be taken to be the date of adjudication, and such order shall have the same consequences and effect as an order of adjudication. 11 U.S.C.A. 207(k)).

APPENDIX C.

Sec. 64. (a) The court shall order the trustee to pay all taxes legally due and owing by the bankrupt to the United States, State, county, district, or municipality, in the order of priority as set forth in paragraph (b) hereof: *Provided,* That no order shall be made for the payment of a tax assessed against real estate of a bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the court. Upon filing the receipts of the proper public officers for such payments the trustee shall be credited with the amounts thereof, and in case any question arises as to the amount or legality of any such tax the same shall be heard and determined by the court.

(b) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment shall be (1) the actual and necessary cost of preserving the estate subsequent to filing the petition; (2) the filing fees paid by creditors in involuntary cases, and, where property of the bankrupt, transferred or concealed by him either before or after the filing of the petition, shall have been recovered for the benefit of the estate of the bankrupt by the efforts and at the expense of one or more creditors, the reasonable expense of such recovery; (3) the cost of administration, including the fees and mileage payable to witnesses as now or hereafter provided by the laws of the United States, and one reasonable attorney's fee, for the professional services actually rendered, irrespective of the number of attorneys employed, to the petitioning creditors in involuntary cases while performing the duties herein prescribed, and to the bankrupt in voluntary and involuntary cases, as the court may allow; (4) where the confirmation of composition terms has been refused or set aside upon the objection and through the efforts and at the expense of one or more creditors, in the discretion of the court, the reasonable expenses of such creditors in oppos-

ing such composition; (5) wages due to workmen, clerks, traveling or city salesmen, or servants, which have been earned within three months before the date of the commencement of the proceding, not to exceed $600 to each claimant; (6) taxes payable under paragraph (a) hereof and (7) debts owing to any person who by the laws of the States or the United States is entitled to priority; *Provided*, That the term "person" as used in this section shall include corporations, the United States and the several States and Territories of the United States.

(c) In the event of the confirmation of a composition being set aside, or a discharge revoked, the property acquired by the bankrupt in addition to his estate at the time the composition was confirmed or the adjudication was made shall be applied to the payment in full of the claims of creditors for property sold to him on credit, in good faith, while such composition or discharge was in force, and the residue, if any, shall be applied to the payment of the debts which were owing at the time of the adjudication. (11 U. S. C. A. 104, prior to amendment of June 22, 1938.)

(N. B. This section is supplied because in effect at time of filing petition in reorganization. The amendment of June 22, 1938, does not affect the rights of the respondents in any different way than does the above.)

APPENDIX D.

RULES OF CIVIL PROCEDURE FOR THE DISTRICT COURTS OF THE U. S.

Rule 75. RECORD ON APPEAL TO A CIRCUIT COURT OF APPEALS.

(a) DESIGNATION OF CONTENTS OF RECORD ON APPEAL. Promptly after an appeal to a circuit court of appeals is taken, the appellant shall serve upon the appellee and file with the district court a designation of the portions of the record, proceedings, and evidence to be contained in the record on appeal. Within 10 days thereafter any other party to the appeal may serve and file a designation of additional portions of the record, proceedings, and evidence to be included.

* * * * *

(h) POWER OF COURT TO CORRECT RECORD. It is not necessary for the record on appeal to be approved by the district court or judge thereof, but, if any difference arises as to whether the record truly discloses what occured in the district court, the difference shall be submitted to and settled by that court and the record made to conform to the truth. If anything material to either party is omitted from the record on appeal by error or accident or is misstated therein, the parties by stipulation, or the district court, either before or after the record is transmitted to the appellate court, or the appellate court, on a proper suggestion or of its own initiative, may direct that the omission or misstatement shall be corrected, and if necessary that a supplemental record shall be certified and transmitted by the clerk of the district court.

* * * * *

(j) RECORD FOR PRELIMINARY HEARING IN APPELLATE COURT. If, prior to the time the complete record on appeal is settled and certified as herein provided,

a party desires to docket the appeal in order to make in the appellate court a motion for dismissal, for a stay pending appeal, for additional security on the bond on appeal or on the supersedeas bond, or for any intermediate order, the clerk of the district court at his request shall certify and transmit to the appellate court a copy of such portion of the record or proceedings below as is needed for that purpose.

APPENDIX E

REVISED RULES OF THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

Rule 13. PRINTED RECORDS

1. When the record is filed, or within 5 days thereafter, the appellant shall file with the clerk a definite statement of the points on which he intends to rely and of the parts of the record which he thinks necessary for the consideration thereof, with proof of service of the same on the adverse party. The adverse party, within 10 days after service of the statement and designation required to be filed by appellant, may designate in writing, filed with thee clerk, additional parts of the record which he thinks material; and, if he shall not do so, he shall be held to have consented to a hearing on the parts designated by the appellant. The parts of the record so designated by one or both of the parties, and only those parts, shall be printed by the clerk. He shall, however, omit all duplication, all repetition of titles and all other obviously unimportant matter, and make proper note thereof. The statement of points intended to be relied upon and the designations of the parts of the record to be printed shall be printed by the clerk with the record. The court shall consider nothing but the points of law so stated and the parts of the record so designated. If at the hearing it shall appear that any material part of the record has not been printed, the appeal may be dismissed or such other order made as the circumstances may appear to the court to require. If either

party shall have caused unnecessary parts of the record to be printed, such order as to costs may be made as the court shall think proper.

* * * * *

6. Certiorari for diminution of the record will not be awarded unless a motion therefor shall be made in writing and the facts on which the same is founded shall, if not admitted by the other party, be verified. All such motions must be made within 20 days after the case is docketed; otherwise the same will not be granted, unless upon special cause shown, accounting for the delay.

(23)

No. 675

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1941

Ralph F. Wiechers, Trustee in Bankruptcy of The Mutual Investment and Security Company, Bankrupt,
Petitioner and Appellee, Below,

vs.

Minnie C. Hansen, Thyra H. Mahrer Behrens, W. J. O'Neill, J. F. McGraw, Catherine J. Hanna, P. B. McAtee, May Walshe, Frances E. Johnston, E. P. Mitchell, Kate A. Mitchell, Margaret Swink, Laura E. Parker, and Albert J. Gould,
Respondents and Appellants, Below.

BRIEF OF THE RESPONDENTS, APPELLANTS BELOW, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

Albert J. Gould,
Attorney for Respondents.

October, 1941

INDEX

		Page
I.	STATEMENT OF THE CASE	1
II.	FACTS	2
III.	ISSUES OF LAW	7
IV.	ARGUMENT	8
	1. Question one of equitable subordination rather than one of creating a priority	8
	Pepper v. Litton, 308 U. S. 295	8
	2. Case one of equitable estoppel to deny contract for voluntary subordination	9
	Bird and Son Sales Corp. v. Tobin, 76 Fed. (2d) 371	9
	3. Numerous questions sought to be raised in petition were not necessary to decision in Circuit Court of Appeals	9
	4. Equitable subordination proper under Chandler Act as under prior acts	10
	5. Rank of lien and priority properly determined in proceedings for that purpose	10
	6. Circuit Court of Appeals correct in considering portions of record suppressed by District Court, but this was not necessary to C. C. A.'s decision as made	12
	7. Argument of opposing petition and brief repetitious	13
V.	CONCLUSION	13

TABLE OF AUTHORITIES

Cases

Bird and Son Sales Corp. v. Tobin, 76 Fed. (2d) 371 9
Pepper v. Litton, 308 U. S. 295 .... 8, 15

Statutes

Chandler Act 10
Rules of Civil Procedure 12

CASE BELOW REPORTED:
121 Fed. (2d) 1011

No. 673

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1941

EARLE F. WINGREN, Trustee in Bankruptcy of The Mutual Investment and Security Company, Bankrupt,
Petitioner and Appellee, Below,

vs.

MINNIE C. HANSSEN, THYRA H. MANKIN BERGER, W. J. O'NEILL, J. F. MCGRAW, CATHERINE J. HANNA, P. B. MCATEE, MAY WALSHE, FRANCIS E. JOHNSTON, E. F. MITCHELL, KATE A. MITCHELL, MARGARET SWINK, LAURA E. PARKER, and ALBERT J. GOULD,
Respondents and Appellants, Below.

BRIEF OF RESPONDENTS, APPELLANTS BELOW, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

STATEMENT OF THE CASE

Trustee Wingren's Petition and Brief are predicated on alleged premises of fact which, it is submitted, no fair reading of the record will support. No reference is had to vital facts on which the Circuit Court of Appeals based its decision. Much stress is placed upon a mass of prolix details irrelevant to determination there or here.

Moreover, the 64-page petition and brief of the Trustee contains 120 citations of cases and 80 citations of statutory sections, Rules of Court and general orders and Text Book pages or sections, resulting in an aggregate of 200 citations of alleged legal authority. So likewise, between its "Questions Presented", "Reasons Relied On", "Grounds of Jurisdiction", "Specification of Errors", "Summary of Argument", and "Argument", petitioner raises no less than 59 numbered points of law allegedly involved in the case.

If all of this does not offend against Rule 38 (2), whereby this Court requires that such a petition and brief be concise, it must at least be regarded as thoroughly confusing the issues on what was, is and should be a relatively simple case.

In view of the Rule last cited, the Court will not wish us in this brief to seek to trace down every lurking error or omission, misstatement, fallacy, or irrelevancy, as we see it, in opposing petition and argument. The simplest and best method seems to be, for purposes of convenience and clarity, to resummarize the Record as already correctly stated in the opinion and both of our briefs in the Circuit Court of Appeals, which restatement of fact will itself constitute an adequate rebuttal to most of the considerations urged in Petition and Brief of opponent.

FACTS

(Op. C. C. A. (10th Circ.) Rec. p. 200-204)
121 Fed. (2d) 1011

Prior to December, 1935, money of the group comprised of Hanssen and others, Respondents here, was stolen, embezzled, or converted by The Mutual Company, subsequent debtor in 77-B and still later the Bankrupt. (Referee Findings p. 45 et seq. Am. Plan p. 17, sec. VIII.)

At the time the Company became a debtor, we claimed that its assets were augmented by the stolen property (p. 120). If this were so, we had a right to follow those

stolen assets in equity, and such a right to follow in equity was a property right unaffected by proceedings in 77-B, or subsequent bankruptcy.

Before we could exercise this right to follow, however, both the debtor Company, and our present real opponents, the Company's voluntary backers and unsecured creditors, more than one-half in value of the claims of which latter group were represented by stockholders and including one director of the defaulting company (p. 155), met us on the threshold and through the statutory forms of the 77-B proceeding, by direct solicitation, or by silent acquiescence, or both, induced us to forego prosecution of our right to try to follow the property in consideration of a lien and priority to be given us whereby the claims of the voluntary backers and creditors in and to the assets of the company were voluntarily subordinated to ours (p. 17 et seq).

We thereupon became eighth in line in the claims against the debtor company, and the voluntary backers and creditors became the ninth in line (p. 17, sec. VIII & IX).

The agreement was embodied in writing and its terms were clear and the confirmation of the Court was jurisdictionally, duly and formally entered in every respect as required by the statute covering the 77-B proceedings (p. 17-26).

Every single creditor who would now benefit should the Trustee prevail against us on this hearing, was duly and formally notified and was a regular and formal party to the afore described proceedings.

The acquiescence to the Plan of Reorganization was by one hundred per cent of such creditors (not 66 2-3%, as intimated in Petitioner's Brief) (p. 22).

After the Confirmation of the Plan, pursuant to the Agreement and Order, thousands of dollars in money and property were released and spent under the first seven sec-

tions of the Plan, in full conformity with the Plan,—all presumably in the interest of the debtor and the voluntary creditors as aforesaid (p. 29-34).

This operation under the Plan continued for a period of nearly three years, during which time we continuously relied on the subordination of the Class IX Claimants, the voluntary creditors. During all this time monies were spent and properties disposed of in respect to which, at least in the limits of good faith possibility, we, the Class VIII Claimants, might otherwise have established our trust fund and equitable property right (p. 29-34).

During this entire period no one (and we particularly refer to the Class IX, voluntary creditors) ever complained that the Confirmed Plan was unfair, inequitable, unjust or should be impeached for any reason, or in any particular.

Eventually, a situation was reached where, to all practical intents and purposes, the first seven sections of the Plan had been entirely performed and nothing remained to be done but to sell certain properties and pay off, first the Class VIII creditors, and then the Class IX creditors (p. 29-34).

By this time the Estate had become insolvent in the sense that it could no longer fully meet both the Class VIII as well as the Class IX claims (p. 29-34).

Shortly thereafter, and in April, 1939, before the bankruptcy, the District Court had found that a delay in payment was in strict conformity with the Plan, and authorized it. No creditor, voluntary or otherwise, interposed objection (p. 26-28).

Prior to that time we, the Class VIII creditors, had received a twenty-five per cent (25%) payment upon our secured claims, as aforesaid, without the slightest objection from any of the voluntary (Class IX) creditors (p. 31, 32).

In this state of the record, in the fall of 1939, and alleging that the delay in payment was due to the difficulties of the Real Estate Market, the Trustee, without any visible promptings of any kind from any creditor, then or ever entitled to any payment, but backed only by the joinder of the admittedly insolvent Company, which had no concern of reality or substance in the controversy then or now, petitioned the Court that the debtor be adjudicated a Bankrupt (p. 29-34).

The reception of this petition by the Creditors was so unfavorable that on November 22, 1939, thereafter, the Trustee and the debtor company further petitioned the Court for leave to withdraw their said petition for adjudication and to procure, in the alternative, a further extension of time within which to make remittances to the creditors under the Plan. No creditors whatsoever, of any class, whether entitled to payment or not, objected in any respect to the request to withdraw the petition for adjudication, or to the request for further extension of time to make payments (p. 121-127).

Notwithstanding the premises, the District Court, thus sua sponte, and on its own motion, as we see it, and with no more ostensible grounds than those hereinbefore appearing, on the 12th day of December, 1939, adjudicated the debtor a Bankrupt and on the 13th day of January, 1940, declined to vacate the order at the petition of the Class VIII creditors, Hanssen, et al, the Respondents here (p. 36-41).

In thus declining to vacate the order, the District Court stated in a written opinion, in substance and effect, that it was not the purpose of the District Court by that decision to adjudicate upon our claim of lien or priority and suggested, as we interpret its opinion, that they be determined by filing claim before the Referee (p. 40).

Thereupon our claim of lien and priority was duly presented to the Referee, thus initiating the proceedings wherein the Trustee now seeks certiorari here (p. 41 et seq).

All parties, and the Referee, the District Court and the Circuit Court of Appeals, have treated the proceeding as one for the determination, on the merits, of the relative liens and priorities of the Class VIII claimants against the Class IX claimants. The Trustee was at all times avowedly representing the Class IX claimants as against us, the Class VIII claimants. In the District Court the Class IX claimants appeared by counsel in support of the Trustee as their representative and in the Court of Appeals they filed a Brief Amici Curiae, likewise in strict support of the position of the Trustee (p. 44-49; 128; 200; 202, 203).

No parties are involved in the Bankruptcy proceeding not previously parties to the Reorganization proceedings. As will be hereafter pointed out, the Trustee-Petitioner is, for the purpose of these proceedings, a representative of the Class IX voluntary creditors, else he has no standing in court at all; since he certainly has no interest in the controversy in any other character.

Nothing is being added to or taken from the Bankrupt's estate. The question is purely one of voluntary subordination of one class of creditors.

It is proper also to emphasize that prior to bankruptcy and until now, except as the contrary may be represented by the petition and brief of the Trustee, herein, there has been no pretense or effort to set aside the lien and priority of the Class VIII claimants as improperly obtained, or inequitable in any particular, but, on the contrary, until the time of the bankruptcy adjudication, it has been consistently ratified by all parties by action based on its existence and validity.

The Court's attention is further drawn to the fact that *even to the present point in these proceedings, the Trustee's petition and brief does not, and cannot, seriously pretend that the decision reached by the Circuit Court of Appeals was other than equitable and just in its ultimate outcome in every moral sense.*

ISSUES OF LAW

As to the issues of law, the Referee treating the issue as well made between the two classes of claimants on the merits, destroyed the lien and priority of the Class VIII involuntary creditors and removed the voluntary subordination of the Class IX voluntary creditors, including stockholders and a director, as aforesaid. The District Court affirmed the Referee.

In this condition the case was brought to the Circuit Court of Appeals and we there contended:

1. That the lien and rank established by the Order of Confirmation was "binding" as a juridical fact in conformity with the statute, and must be so treated on subsequent bankruptcy.

2. That even if it was not so binding as an adjudication, still it was binding as a contract for subordination, legally and judicially sanctioned under the facts as given.

3. That even if it were not binding in either of the two ways aforementioned, nevertheless under the peculiar facts of this case, the Court was bound to treat it, on doctrines of laches and equitable estoppel, as though it were so binding, that all parties to the situation had so treated it; and that it was impossible to restore us to our status-quo-ante the proceedings.

In other words, we urged that *even if there were not, in fact, a specific binding contract for subordination on the part of the Class IX creditors, they were, nevertheless, now estopped to deny that such was the fact.*

In substance and effect, the Circuit Court of Appeals, as will appear from the opinion, held that it was unnecessary to decide either of the former two contentions, (1) and (2), since the Court was prepared to hold with us on the last, (3) (Op. C. C. A., Rec. p. 202, 203).

It seems to us that the decision is manifestly correct. It is the only ruling which this record offers for review by this Court.

ARGUMENT

Having thus restated the facts in the record, it must be abundantly evident that the dominating fallacy of the Trustee's petition and brief is to set up alleged "questions of law" predicated on facts having no basis at all, or a basis incorrectly stated, on such record.

Many of petitioner's points are repetitious in substance and, for brevity, these may be grouped.

1. On the merits, recurrent contention of Trustee Petitioner's petition and brief is to the effect 'that the Circuit Court of Appeals "created a priority" thereby defeating the express statutory regimen.' (Petitioner's "Questions" 2 and 3, p. 10, 11, et al, Pet. & Bf.)

This is not the fact. The Circuit Court of Appeals used its clear equitable and statutory powers to subordinate one claimant, or group of claimants, on the equitable considerations existing between the claimants themselves.

> "Certainly, if, as provided . . . a claim which has been allowed may later be rejected in whole or in part according to the equity of the case, *disallowance or subordination in light of equitable considerations may originally be made.*" (Italics ours.)
>
> *Pepper v. Litton,*
> 308 U. S. 295, 308.

Sometimes the Petitioner's contention under present discussion takes the form of assuming that the Circuit Court of Appeals gave us preferences solely by reason of the original embezzlement of our funds.

Such an assumption is wholly unwarranted on the record. We do not claim and the Circuit Court of Appeals did not hold that our lien and priority arose only from the embezzlement of our funds, but rather from the voluntary self-subordination of the voluntary creditors whereby we were lulled into security and lost the means of *following our embezzled funds.*

2. Petitioner's brief next intimates, or states, on several occasions that a bankruptcy creditor can lawfully be subordinated "only for moral turpitude".

We do not think the Chancellor's limitations are so confining:

It seems obvious that, if creditors can voluntarily subordinate themselves by an express contract without offending against the Bankruptcy statute (*Bird and Son Sales Corp. v. Tobin,* 76 Fed. (2d) 371, 373, 100 L. R. A. 654), then they can equally subordinate themselves by acts and omissions which, under equitable principles, estop them to deny the status that such an express contract would have established.

3. The Petitioner's questions numbered 6 to 11, inclusive, are imported vi et armis into this record as hypothetical and moot questions which the Circuit Court did not decide, and had no need to decide, and which the Record itself, therefore, does not offer for determination here.

It may be sufficient to say that the Circuit Court did not hold and did not need to hold that the debtor's assets were, in fact, augmented by the embezzlement, because the voluntary backers in practical effect conceded as much (insofar as they were concerned), by willingly giving lien and priority predicated on that theory.

As formerly stated, the Circuit Court did not hold that a mere assertion of a trust relationship gives a priority, because, on the facts of this case, the assertion of the trust

relationship was followed by a claim of augmentation of assets and a voluntary acknowledgment that such claim was at least contestible—this by the voluntary subordination of the voluntary backers, as aforesaid.

The Circuit Court expressly declined to determine the effect of the Confirmed Plan as a contract, or judgment, beyond the equitable subordination of the voluntary backers on the particular facts of the case.

4. The Trustee, by his questions 12 and 13, seeks to import the Chandler Act, in some especial aspect, into this controversy. In the Chandler Act, as in every other bankrupty statute, claims may be subordinated on equitable principles, and that is what was here done. Other questions on the Chandler Act are moot at this point in the controversy.

The Trustee's somewhat complicated sixth question (Petition and Brief, p. 11, 12), if we understand it, draws out of thin air a legal issue never raised by any party below and on which there is no occasion for controversy. Answering it as we understand it, the Class VIII claimants readily agree that they are bound by acquiescence in the Confirmed Plan (the same as they assert that the Class IX claimants are bound), and it is now, not only physically and legally impossible for them to assert their original right to follow trust property as it existed prior to the Plan, but also they have never desired, or pretended, to have a right to do so after their acquiescence in the confirmation of the Plan. Our only contention is that the Class IX claimants are similarly bound, and such is the decision of the Circuit Court of Appeals.

5. Petitioner's position in newly-taken procedural aspects of his argument (Question 1, p. 10, Petition and Brief) seems to be:

'That the Court should not have subordinated the Class IX claimants except in a proceeding for an order of distribution rather than on the proceeding actually adopted for

the determination of the nature of the claims of the Class VIII claimants.'

It will be noted at once that this position of the Trustee is highly technical and has no foundation in substantial justice. The voluntary Class IX creditors were represented (and perhaps too thoroughly represented, considering his supposedly neutral position as an officer of the District Court, and that these proceedings are at the expense of the Bankrupt's estate), by the Trustee himself in the present proceeding for the determination of lien and priority of our claim.

In addition to that, Class IX claimants had their own counsel in the hearing before the District Court, were in the Circuit Court of Appeals and filed briefs as amici curiae—their argument in each case being practically identical with that of the Trustee.

Every one concerned, including the Referee and Courts, treated our claims from inception as specifically designed for the determination of the relative lien and priority of the two classes of creditors.

At this late stage, therefore, to assert that we should have waited to litigate our lien and priority until a question of distribution, would be to make a mockery of the whole proceedings.

Indeed, if the Trustee was not and is not at all times representing the Class IX claimants as against us in this proceeding from its inception, then it is difficult to see how he would have any standing, even in this Court at this time, since the Bankrupt's estate is manifestly affected in no other particular than by a determination of the relative rank of the two groups of creditors.

It is safe to assert that if we had attempted to defer the litigation of our lien and priority to the time of a final distribution order, the Trustee would have been the first to

say that such would be too late and that we had lost our rights by such delay.

In fact, this Court will note the obvious inconsistencies in the position of Trustee-Petitioner wherein he asserts, in one breath, that we are already too late in litigating our position, which he now claims was adjudicated against us by the mere bankruptcy adjudication (p. 46, 47, Trustee's Brief); whereas, in the next breath, he asserts that we are premature in the respect that our rank and lien should be determined on a later proceeding for distribution.

Manifestly, the Petitioner Trustee cannot be right on both wings of his inconsistency. We think he is wrong on both and that the rank of the classes were and are properly adjudicated in the determination of our claims upon the proceedings specifically brought for that purpose and acted upon by the Referee and both lower courts as appropriate for such.

6. The Trustee's remaining questions 14 to 16, seek to evoke obiter from this Court condoning the action of the District Court in suppressing praecipaed veritable parts of its own record in the cause (p. 13, 14, Pet. & Bf.).

If the Circuit Court of Appeals considered the suppressed portions of the record, the Circuit Court of Appeals was most manifestly within its rights under the "Rules of Civil Procedure" promulgated by this Court.

Yet, the Circuit Court's opinion could have been, and perhaps was, made on the record without those suppressed portions.

The fact of the trust-fund-conversions (main substance of the suppressed record) appears in the very findings of the Referee, which the Trustee Petitioner sought, and seeks, to sustain,—this in addition to a very clear intimation of the fact from the Plan itself.

The other parts of the diminished record bore only on the alleged abuse of discretion of the District Court. As to whether or not the District Court abused its discretion in these proceedings, the Circuit Court did not need to decide and, therefore, did not decide.

7. The portion of Trustee-Petitioner's Summary and Argument under Roman Numeral II, on page 25 of his Brief, is a mere repetition of his Argument in the Circuit Court of Appeals and is, as we submit, satisfactorily answered in the opinion of the Circuit Court of Appeals as well as by our Reply Brief, therein, both appearing in the transcript on file here (Rec. p. 200-204; 185-199).

As previously indicated, it would serve no good purpose to examine the many cases cited in Trustee-Petitioner's Brief, none of which are subjected to an analysis of fact, or even used for purposes of quotation, and, as to which, it is safe here to state that they do not militate in any degree against the correctness of the decision rendered by the Circuit Court of Appeals in this cause.

CONCLUSION

Without going into further detailed discussion of Petitioner's petition and brief, it is sufficient to submit that the foregoing considerations indicate:

1. That there is no novel question presented on this record;

2. That there is, on this record, no question of bankruptcy which has not been already settled by this Court;

3. That the decision of the Circuit Court of Appeals conflicts with that of no other Circuit Court;

4. That it is amply sustained by the decisions of this Court cited in the decision of the Circuit Court of Appeals;

5 and 6. That it is not in conflict with any decision of this Court;

7 to 9. That there has been no departure from accepted judicial procedure.

The foregoing obviates the necessity of further specific reference to the "Specification of Errors", "Summary of Argument" and "Argument", all of which are repetitious in respect to law points presented.

We conclude, as in the Circuit Court of Appeals, that the plain and simple facts of the case speak for themselves, amply to justify the decision of the Circuit Court of Appeals under question here:

A defaulting company steals specific property from certain of its principals. When these victims try to follow their property in 77-B proceedings, they are met by the debtor itself and voluntary backers and creditors of the defaulting company who induce the victims to give up their equitable right to follow their property in consideration that they should thereafter have a lien and priority to secure the return of the stolen money and that the voluntary backers and creditors would voluntarily subordinate themselves for this purpose.

This arrangement is promulgated and accepted by all parties in interest, including the real parties in interest now here, with full and fair consideration and due formality, and is thereupon approved by the District Court with full jurisdiction and in strict statutory form as fair and equitable in every particular.

The fairness and equity of the solemn property settlement thus unanimously agreed upon and the equally solemn

unappealed Confirmatory order of the District Court have never to this day been attacked.

The same parties who promulgated the program, however, are now the real parties in interest as represented by the Trustee in this Court, still seeking, on technical grounds, notwithstanding a full and careful determination by the Circuit Court of Appeals, a repudiation of the very arrangement by which they have already, for their benefit, obtained two and a half years delay, thus palpably defeating any possible reclaim proceedings by the defrauded victims of the Bankrupt, paid off thousands upon thousands of dollars more in administration fees paid either directly or indirectly, at least in presumption of law, to their benefit.

No amount of elaborate argument can conceal the facts just hereinbefore stated. It is little wonder that the Circuit Court of Appeals has declined to lend itself to any such inequitable program of the Trustee; but, rather, has invoked the dictum of this Court:

> "They (equitable powers of Bankruptcy Courts) have been invoked to the end that fraud will not prevail, *that substance will not give way to form, that technical considerations will not prevent substantial justice from being done.*" (Italics ours.)
>
> *Pepper v. Litton,*
> 308 U. S. 295, 308.

Respectfully submitted,
ALBERT J. GOULD,
Attorney for Respondents.

SUBJECT INDEX

	PAGE
Statement of the Case	1
Compliance with Rules of Court	2
Facts	2
Argument:	
1. *Pepper vs. Litton* has been improperly applied	4
2. No equitable estoppel has been shown	6
3. Petitioner entitled to argue all questions which the court refused to determine below, in connection with application for writ on the grounds stated in "Reasons" numbered one to seven, inclusive	7
4. Decision of Circuit Court conflicts with *Rude v. Buchhalter* on the procedural question	7
5. Respondents have shown no cause why the writ applied for should be denied	7
Conclusion	10

CASES CITED

Bird and Son Sales Corp. vs. Tobin, 76 Fed. (2) 371, 100 A. L. R. 654	6
Buchhalter vs. Rude, 54 Fed. (2d) 834	8
Davis v. Louisville Trust Co., 181 Fed. 10	3
Geist v. Prudence Realization Corp., 122 Fed. (2d) Adv. Op. No. 4, p. 503	9, 10
In re Carden, 118 Fed. (2d) 677	9
In re Columbia Ribbon Co., 117 Fed. (2d) 999	4, 5, 7, 9
Pepper v. Litton, 84 L. Ed. 281, 308 U. S. 295	4, 6
Rude v. Buchhalter, 286 U. S. 451, 76 L. Ed. 1221	8, 9
So. Pac. v. Bogart, 250 U. S. 483, 63 L. Ed. 1099	10
U. S. v. Killoren, 119 Fed. (2d) 364	9

STATUTES AND RULES CITED

PAGE

Chapter X of the Chandler Act:
Article XII, Sec. 236 (11 U. S. C. A. 636) 4
Article XII, Sec. 238 (11 U. S. C. A. 638) 7

Rule 27, Revised Rules of the Supreme Court of the United States 2

Rule 38 (2), Revised Rules of the Supreme Court of the United States 1

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941

No. 673

EARLE F. WINGREN, Trustee in Bankruptcy of The Mutual Investment and Security Company, Bankrupt,
Petitioner and Appellee Below,

vs.

MINNIE C. HANSSEN, THYRA H. MANKIN BERGER, W. J. O'NEILL, J. F. McGRAW, CATHERINE J. HANNA, P. B. McATEE, MAY WALSHE, FRANCES E. JOHNSTON, E. F. MITCHELL, KATE A. MITCHELL, MARGARET SWINK, LAURA E. PARKER and ALBERT J. GOULD,
Respondents and Appellants Below.

REPLY BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT.

STATEMENT OF THE CASE

Compliance with Rules of Court

Respondents would make it appear, by means of misleading numerical statistics compiled by them from petitioner's petition and brief, that petitioner has violated Rule 38 (2) of this court. Compliance with that rule as

to the contents of the petition, and with Rule 27 as to the form and substance of the brief, necessitates some repetition in the brief of matter stated in the petition. The fact is, the sixteen propositions stated in the petition (Pet. pp. 10-14) are specified as eight points (Br. pp. 22-24), and the argument thereof covered in twenty-seven pages (Br. pp. 26-52). Of the total sixty-four pages, ten constitute the appendix of statutes required by Rule 27 (f). The complexity of the problems involved, and the necessity of repeated reference to the many sections of the bankruptcy act which are applicable, permit no less.

Facts

It is submitted that respondents' brief is, in fact, no answer at all, either in opposition to the issuance of the desired writ, or in refutation of the propositions of law stated. It contains principally simple denials of some of the arguments of petitioner, no attempt at analysis or discussion of the authorities cited, and the citation of only two cases, both of which have been clearly distinguished in petitioner's brief from the case now before the court.

Both by direct statement and inference, respondents have implied that each of them had claimed augmentation (their brief, pp. 2, 10, 12, 14), citing one of the documents (R. 120) excluded from the record by the District Judge (R. 69-71) wherein it appears that *two* of the creditors had claimed augmentation. The position of these two creditors is not typical of all creditors mentioned in Section VIII, nor indeed even typical of all of respondents (See R. 159, 214-16).

Respondents have repeatedly used the words "voluntary backers" in referring to the creditors included in Section IX of the plan (See pages 3, 4, 7, 9, 14, 15, Res. Br.). The use of such words is intended to discredit the position of Section IX creditors and place upon them responsibility for respondents' situation (See pp. 3, 9, 14, 15, Res. Br.) which is not rightfully theirs. Cited as support for such statement is an explanation of the facts

appearing in petitioner's brief below (R. 155) which actually disposes effectively of any such contention (See also Pet. Br. p. 34).

On pages six and eleven of respondents' brief the statement is made that the class IX creditors appeared by counsel in this matter, the inference being that all the Class IX creditors voluntarily appeared; this is untrue (See R. 65, 70, 71, 128-9, and especially 154-5, wherein the status of the claims of creditors represented by amici curiae is correctly described). The voluntary appearance of some of the general creditors in this controversy does not amount to the appearance of all, and where the issues are not properly formed, does not justify the entry of an order determining the ultimate rights of all the creditors. *Davis* v *Louisville Trust Co.*, 181 Fed. 10 (6th C.C.A. 1910).

At the bottom of page six of their brief, respondents make the astounding statement that petitioner does not pretend that the decision of the Circuit Court of Appeals was unjust. Petitioner vehemently denies that there is any equity or justice in it, "in any moral sense" or otherwise. The summary statement preliminary to the petition for the writ calls attention to the inequitable result of the decision (Pet. p. 1), the point is raised in Question numbered 4 (Pet. p. 11), specified as error in points numbered 1 and 3 (Pet. p. 22), and argued in Section I, subparagraph (d) (Pet. pp. 31-32). It was also argued in the brief in support of petition for rehearing (R. 210-214).

ARGUMENT

1. *Pepper* v. *Litton* has been improperly applied.
2. No equitable estoppel has been shown.
3. Petitioner entitled to argue all questions which the court refused to determine below, in connection with application for writ on the grounds stated in "Reasons" numbered one to seven inclusive.

4. Decision of Circuit Court conflicts with *Rude* v. *Buchhalter* on the procedural question.

5. Respondents have shown no cause why the writ applied for should be denied.

1. Respondents state (their brief p. 8) that the Circuit Court used "its clear equitable and statutory powers" to subordinate one group of claimants on the equitable considerations existing between the claimants themselves, and that no priority has been created, but they have failed to answer the argument denying the power of the Circuit Court, *either* to subordinate or grant a priority in this case (Pet. Br. pp. 26-37), and have cited no contrary authorities. They have ignored *In re Columbia Ribbon Company*, infra, which is precisely in point, where the question arose under an adjudication under Section 236, Chapter X, in proceedings initiated under Section 77 B, exactly as here. The Court said:

> "As we have seen, Section 238 directs that the proceeding be conducted 'so far as possible, in the same manner and with like effect' as if the petition for reorganization had been an ordinary involuntary bankruptcy petition and the approval of the petition an adjudication of bankruptcy. It follows that the court in determining the priority of claims against the estate is bound by the provisions of Section 64, sub. a, as amended, 11 U. S. C. A. Sec. 104, sub. a, which specify the classes of debts which are to have priority of payment over general creditors of a bankrupt estate and the order of their payment with respect to each other. Five classes of debts having priority are established. The first class includes 'the costs and expenses of administration.' Since Congress has set up no order of priority within the first class the court may not fix priorities within the class. Missouri v. Ross, 299 U. S. 72, 57 S. Ct. 60, 81 L. Ed. 46; Missouri v. Earhart, 8 Cir., 111 F. (2d) 992, certiorari denied 61 S. Ct. 43, 85 L. Ed. . . .

"The referee and the court below grounded their action in granting priorities within the class of administration expenses upon what they believed to be the equitable powers of a court of bankruptcy. It is well settled, as the Circuit Court of Appeals for the Fourth Circuit pointed out in Westall v. Avery, 171 F. 626, 628, 'that bankruptcy proceedings themselves are purely equitable in their character, and, within the limits prescribed by the Bankruptcy Act (11 U. S. C. A. Sec. 1 et seq.) and the special rules of practice prescribed by the Supreme Court, are to be administered in accord with the general principles and practices of equity.' See Local Loan Co. v. Hunt, 292 U. S. 234, 54 S. Ct. 695, 78 L. Ed. 1230, 93 A. L. R. 195. But these equitable powers are to be exercised within the limits laid down by the Bankruptcy Act and subject to its specific provisions. In re Concentrated Products Corp., 3 Cir., 38 F. 2d 745. The court may not by granting a priority which it deems equitable set aside the clear congressional mandate that no such priority shall be accorded. Pepper v. Litton, 308 U. S. 295, 60 S. Ct. 238, 84 L. Ed. 281, which was relied on by the referee and court below, is not to the contrary. That case holds that a court of bankruptcy under its equitable powers may disallow or subordinate a particular claim in bankruptcy, which because of the fraudulent nature of the claim or the bad faith or improper conduct of the claimant, ought not in equity and good conscience to be allowed or paid on a parity with other claims. It does not hold that the court may set up a subclassification of claims within a class given equal priority by the Bankruptcy Act and fix an order of priority for the sub-classes according to its theory of equity. . . .

In re Columbia Ribbon Co., 117 F. (2d) 999, 1001, 1002.

That *Pepper v. Litton* presented a different question appears from Mr. Justice Douglas' own statement at the beginning of the opinion:

> "The case presents the question of the power of the bankruptcy court to disallow either as a secured or as a general or unsecured claim a judgment obtained by the dominant and controlling stockholder of the bankrupt corporation on alleged salary claims."

Subordination of the claim of a creditor because of his own fraudulent conduct, where the creditor is before the court and the issues are properly framed, is quite a different thing from subordination of the claims of an entire class of creditors who are not before the court, and where no issues bearing on the equitable considerations existing between the claimants themselves have been presented. *Pepper* v. *Litton* certainly is not authority for the proposition that a Circuit Court has the power to inquire into the validity of one claim, and on that inquiry subordinate claims not before it on the appeal. *Pepper* v. *Litton* is merely an application of the principle of clean hands; the record here contains no facts calling for such application.

It clearly follows that the Circuit Court decided this case in a way not in accord with applicable decisions of this court and in conflict with principles established by this court.

2. Respondents state at page nine of their brief that petitioner "intimates, or states, on several occasions that a bankruptcy creditor can lawfully be subordinated 'only for moral turpitude'." There is no such statement in petitioner's brief.

Petitioner devoted considerable space to an analysis of *Bird and Son Sales Corp.* v. *Tobin*, 76 Fed. (2nd) 371, 100 A. L. R. 654 (Br. pp. 33-4) for the express purpose of pointing out that notice was given to all creditors

before decision by the court. Respondents have ignored this important feature, and merely cite the case to show that creditors *can* voluntarily subordinate themselves by acts and omissions which, under equitable principles, estop them—a general statement which is undoubtedly true, but which has no application to this case.

3. Since petitioner does not know, and cannot conclude from the opinion, on what "equitable considerations" the Circuit Court subordinated the Section IX creditors, he has argued each ground on which the Circuit Court might have based such subordination. The necessity of so doing sufficiently answers any charge of inconsistency in the argument of petitioner, and there can be no question of petitioner's right to argue such points, as well as all those questions which the Circuit Court expressly refused to determine, in connection with his application for writ on the grounds stated in "Reasons" numbered one to seven (Pet. pp. 14-17).

Respondents now claim that questions involving the Chandler Act are moot. They were argued at length in all the briefs below, and are the proper subject of argument by petitioner in this case where the application for the writ is based squarely on the refusal of the court to apply the plain mandate of the bankruptcy act. For example, the application of Section 238, Chapter X, is one of the vital points of the controversy. Cf. *In re Columbia Ribbon Company*, infra, pp. 4-5.

4. Apparently respondents' view is that the questions relating to the power of the Circuit Court to render the decision handed down may not now be raised, since not argued below. These questions never arose until the decision was rendered—no issues were formed nor evidence introduced either calling for or permitting a decision by the Circuit Court on the basis adopted; they were first presented to the court in Petition for Rehearing which is the earliest they could have been raised on the record as made (R. 207-18).

This is not the first time the Circuit Court of the Tenth Circuit has erroneously attempted to exercise equitable powers and has gone beyond the issues presented by the record. In *Buchhalter* v. *Rude*, 54 Fed. (2nd) 834, the court imposed certain conditions in the decree which "appeared" to the court "to be equitable" (p. 839). Certiorari was granted, and the decision modified in *Rude* v. *Buchhalter*, 286 U. S. 451, 76 L. Ed. 1221. The court said:

> "The Circuit Court of Appeals went beyond the issues presented by the record. Its opinion shows that determination of the appeals did not require findings as to the good faith of petitioner. . . . And petitioner had no reason to apprehend that any such matter would be considered on either appeal. He had no opportunity to be heard in respect of the authority of the court to make such an allowance or as to the facts touching the propriety of basis of the same. Petition for rehearing and denial, as here, upon a reasoned opinion may not in such a matter fairly be regarded as the equivalent of a hearing in advance of decision." (286 U. S. 460, 76 L. Ed. 1225.)

How much less, then, can it be said that the Section IX creditors have had a hearing in advance of decision in this case, where, after petition for rehearing filed, no additional opinion was filed.

Questions relating to the validity of respondents lien were properly raised in the circuit court; the court, on the issues before it, should have decided whether they did or did not have a lien; it refused so to decide, but went beyond the issues and rendered a decision on questions not before it. Respondents have never attempted to form issues before any court on the question of the existence or non-existence of such equities; in their reply brief in the Circuit Court they insisted (R. 187-190) that they claimed a lien, not a preference or priority.

On the record, the decision was plainly in conflict with the principles established by *Rude* v. *Buchhalter, supra.*

5. Respondents have failed to demonstrate any reason for the refusal of this court to grant the writ applied for.

It is noteworthy that in conclusion of their brief (pp. 13-15) they deny categorically that any of the reasons stated by petition for the granting of the writ exist, and allege that there is no question of bankruptcy which has not already been settled by this court, and that the decision is amply sustained by the decisions cited therein; yet no cases are mentioned wherein the questions raised by this record have been decided adversely to petitioner.

It is noteworthy that respondents allege that the decision of the Tenth Circuit conflicts with that of no other circuit court, and yet no attempt is made to reconcile the decision of this court with the two cited by petitioner as being in conflict, i. e., *In re Columbia Ribbon Co.*, 117 Fed. (2nd) 999 (3d Cir. 1941), and *In re Carden*, 118 Fed. (2) 677 (2d Cir. 1941) (Pet. Br. pp. 15-16, 29, 31, 48). Since the filing of that brief, another case has been noted wherein the Eighth Circuit expressly approved the conclusions of *In re Columbia Ribbon Co., supra;* it is *U. S.* v. *Killoren*, 119 Fed. (2d) 364, wherein are also cited many other cases on this point mentioned in our first brief.

On October 20, 1941, there was published a new decision of the Second Circuit which is directly in point on the question of subordination on equitable considerations. Therein the court said:

> ". . . . Similarly, Bankruptcy Act, Sec. 65, sub. a, 11 U.S. C. A. Sec. 105, sub. a, requires, in liquidation, the distribution of 'dividends of an equal percentum' 'on all allowed claims, except such as have priority or are secured.' Moore v.

Bay, 284 U. S. 4, 52 S. Ct. 3, 76 L. Ed. 133, 76 A. L. R. 1198; Globe Bank & Tr. Co. v. Martin, 236 U. S. 288, 305, 35 S. Ct. 377, 59 L. Ed. 583; Sampsell v. Imperial Paper & Color Corp., 61 S. Ct. 904, 907, 85 L. Ed. ——. The only departures made from the ordinary rule of equality are based on some very definite equity, such as fraud, Pepper v. Litton, 308 U. S. 295, 60 S. Ct. 238, 84 L. Ed. 281, mismanagement of the debtor by a parent corporation, Taylor v. Standard Gas & Elec. Co., 306 U.S. 307, 59 S. Ct. 543, 83 L. Ed. 669, or concealment of a claim to the prejudice of another creditor, In re Bowman Hardware & Electric Co. 7 Cir., 67 F. 2d 792. In the absence of such an equity, subordination is not a function of the bankruptcy court. Crowder v. Allen-West Commission Co., 8 Cir., 213 F. 177, 184; Sampsell v. Imperial Paper & Color Corp., supra; cf. Moise v. Scheibel, 8 Cir., 245 Fed. 546." *Geist* v. *Prudence Realization Corp.* 122 Fed. 2d) Adv. Op. No. 4, p. 503, 505-6.

CONCLUSION

It is submitted that the purpose of the Circuit Court should have been to declare and enforce the bankruptcy law on the questions raised before it on appeal, not to punish the Section IX creditors (cf. *So. Pac.* v. *Bogart*, 250 U. S. 483, 63 L. Ed. 1099, 1109), nor to authorize the unjust enrichment of the Section VIII creditors at the expense of Section IX creditors who are not before the court and have never had an opportunity to be heard. Such is the effect of the decision of the Circuit Court. It constitutes such a radical departure from the accepted course of judicial determination as alone to demand (without regard to the many other valid reasons for granting the writ) the exercise of the powers of supervision of this court.

Respondents have presented no valid reason for the denial of the writ; they have cited no authorities authoriz-

ing its refusal; we respectfully submit that this cause should be reviewed and determined, and upon final hearing, the judgment of the Circuit Court of the Tenth Circuit reversed.

Denver, Colorado, October 31, 1941.

JOHN W. SHIREMAN,
NORMA L. COMSTOCK,
NORMAN H. COMSTOCK,

Attorneys for Petitioner.